SELECT COMMITTE ON CONSUMER CREDIT

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THE CHAIRMAN: We will now call the meeting to order. This morning we are to hear from Professor Donald C. MacGregor, Professor of Economics, University of Toronto. I understand that you are not speaking from a prepared brief this morning but you wish to make some general remarks, or don't you, before some of the members proceed with perhaps some questions that they might have?

MR. MacGREGOR: Mr. Chairman, and gentlemen, my position is that I don't come here as a petitioner but rather on invitation. I would like to have a written statement of everything I want to say but I've had a busy time since early this month when this was first mentioned to me, so all that I have are a number of partly written statements and notes.

In any event I have been led to believe that you are mainly interested in asking a number of questions and it seems to me that very likely the questions would develop in the course of the session and that I couldn't anticipate them all at any event. I have a number of questions set down in Mr. Irwin's letter of the 21st September, which was directed to the Head of our Department and this was, in due course, turned over to me. And finally it was arranged that I be the one to attempt to answer them.

That is the reason I say I am not here as a petitioner. I'm here as an answerer.

Perhaps I should read the questions that were asked just to refresh your memories. I had these questions again by telephone but I think it might be

better to read them from the original letter.

THE CHAIRMAN: Yes, because I think the other members really wouldn't know what those questions are.

MR. MacGREGOR: This is the letter directed to Dr. Eachbrook, who is the Chairman of the Department. Can I be heard back there? I've spent quite a bit of time in this room and I know there are some difficulties in hearing.

To Dr. Eachbrook: The Chairman of the Select Committee on Consumer Credit considers it to be desirable to hear the views of an economist in regard to the subject matter into which the Committee is inquiring. Then there is a paragraph on the terms of reference that I need hardly read.

Some of the key problems which have been revealed and which the Committee must resolve or evaluate are (1) Feasibility of calculating and expressing the cost of borrowing in terms of a rate percent per annum; (2) Economic implications of legislation which might (a) require universal expression of the cost of borrowing in terms of a rate percent or some other statute form, (b) provide limitations in respect to down payments and right of repossession, a cooling off period, standard forms of contract warranties, etc. These two questions.

Then going on to another paragraph to elaborate. It has been suggested that economic effects might take the form of (1) a decline in credit buying with implications for production, employment and economic

better to read them from the original letter.

THE CHAIRMAN: Yes. However I think the other members really wouldn't know what these questions were.

MR. [illegible]: This is the summary distributed by Dr. [illegible], one of the [illegible] of the Department. [illegible] quite a bit of time [illegible] and [illegible] there are some difficulties in [illegible].

So Dr. [illegible]: The [illegible] of the [illegible] on [illegible] [illegible] it to be desirable to reach some sort of an agreement in regard to the subject matter as to scope and magnitude is important. Then there is a [illegible] as the [illegible] of procedure that I have [illegible].

Some of the key problems which have been reviewed and which the Committee may [illegible] on occasion are (1) possibility of establishing and specifying the [illegible] of [illegible] in terms of a [illegible] percent per annum. (2) Economic justification of legislation which might (a) require [illegible] of the risk of [illegible] in terms of a rate per annum or some other adequate form, (b) provide flexibility in respect to such [illegible] for rights of [illegible], a cooling off period, standard forms of contract warranties, etc. These two questions.

Then going on to another paragraph [illegible] standards. It has been suggested that [illegible] might take the form of (1) a section in [illegible] with [illegible] for [illegible], [illegible] and [illegible]

statutes; (2) transfer of the cost of buying to the price of the article; (3) realignment within the lending industry -- that is to say, more borrowing from institutional lenders and less from private lenders; (4) reaction to business -- I take it this means presumably adverse reaction of business to the change. And (5) reaction of the public -- which I take it again implies an adverse reaction of some kind.

As to the first question on the feasibility of calculating and expressing the cost of borrowing, I take it that you have looked into this and have had some opinions by people who are skilled in making interest calculations by different methods, and that you have the answer to that one. At any rate as far as choice of methods. I am aware that there are various ways of doing this, although I am not able to explain them. All that I would care to say about this is that while no one method is superior in every respect, any agreed upon method which will enable reasonably good comparisons between different offerings seems to have an advantage. I have here, for example, the results of a study which was published last year, a consolidation of earlier studies and some updating on new automobile finance rates in the United States, between 1924 and 1962, by Robert B. Shea, of the staff of the National Bureau of Economic Research. This necessarily employs standard methods of calculating the rates. You can't make comparisons between the rates offered by different companies nor rates over a period of almost forty years without using some reasonable

common yardstick, which is the method employed.

There is somewhere here the formula which was adopted for this purpose -- it is not given a name, the formula is simply presented. It is known as the constant ratio formula which is described in a later paragraph, and that is used throughout. This is a useful study for quite a number of reasons. It shows the extent of the difference in rates according to the type of lender for different parts of the country. But more especially it shows the course of rates over this rather long period and indicates that prior to the middle thirties the rates were considerably higher than they have been since that time. Since the middle thirties the rates don't seem to have changed a great deal except that they have undoubtedly moved up and down with the rates for other lending, not immediately but looking at it over the years, there is a fairly close relation between the rates for auto financing in the United States and the short term business loan rates and even with the long term corporate bonds.

The value of some uniform method is well explained in this and I would doubt whether the rather fine distinctions that are made by opponents of this method would count for very much in the minds of people who want to get at least some idea of what they are paying.

I find that even in connection with mortgages there is a difference between Canadian and American rates. In recently sending away to a well

common variation, which is the natural [illegible],

[illegible]

which was adopted from this [illegible] -- it is not given

a name; the formula is [illegible]. It is

known as the [illegible]

described in a [illegible] paragraph, [illegible]

throughout. [illegible]

of reasons, [illegible] the difference in

[illegible] according to the [illegible]

[illegible]

[illegible]

[illegible]

[illegible] considerably [illegible]

[illegible]

[illegible]

[illegible]

[illegible]

over the [illegible]

[illegible]

[illegible]

with the [illegible].

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

the period.

[illegible]

[illegible]

[illegible]

known firm in Boston to have some mortgage calculations made, I noticed I was asked whether I wanted it done by the American or Canadian method. Not quite knowing which was which I decided I had better say Canadian method -- for what I was going to get I decided I had better say Canadian method. I'm not able to explain the difference in that one -- this is in serial mortgages where there is a standard payment, blended payment month by month.

Now as to the second much larger and more complicated question of the economic implications of legislation. At this point there is a danger that I may indulge in a professorial lecture. If I had presented you with a written statement it would have taken something of that form.

I'm going to risk the danger, at any rate for just a few moments, and make a few comments on the market, as they seem to relate to the supply of funds -- as they seem to relate to whatever market there is for consumer credit.

The argument that things can be left to run themselves -- the laissez faire argument -- depends very largely, rests very largely on the assumption that there is a more or less perfectly competitive market in this field and if it is found that that assumption is not true in all respects then the argument is weakened. I don't say it vanishes, but it is not as strong, perhaps not as generally applicable.

Now the conditions for a perfectly

competitive market can be expanded at great length, but all I want to do is point to some fairly obvious things. First of all there must be many buyers, many takers, a sufficient number, that is to say, so that no one buyer can depress the price by withholding his purchases. Now there is no doubt about it in this case that there are many buyers, many people think there are too many buyers, too many users of consumer credit. There is no question there, as to the number of persons on the purchasers' side of the counter, the counter is crowded.

Second, there must be many suppliers. In the case of manufacturing we speak of producers but here we speak of suppliers or sellers of money, they are in this case renters of money rather than sellers of it. There must be a sufficient number, that is to say, so that individual lenders cannot raise the price of money by withholding his funds from the market. If it is true there are a sufficient number of lenders who make it impossible for any one lender to raise the price, I am not able to say. Especially when one remembers that the market is not for a single type of accommodation but a number of types of accommodation. I don't express any opinion on that. You are in a position to express an opinion and I think it would be a mistake for me to attempt to. Whether you think it is a perfectly competitive market, whether there is a sufficient shortage of lenders so that there may be some monopolistic influence.

The product of service which is offered

-- in this case the use of money,and I think I would stress here money as well as its use -- but about equal emphasis to money, the thing which is made available, and the use of it, -- must be of a uniform or standard type. That is to say, undifferentiated or homogeneous, so that any unit of the product may be substituted for any other unit, irrespective of the maker or vendor. In other words -- I'm going to repeat -- the thing which is sold must be completely substitutable.

Now, this implies uniformity not only in the thing itself, which is money -- for which there could hardly be anything more uniform, one dollar bill is substitutable for another dollar bill -- it's a perfect example of substitutability. In addition to that, however, there must also be uniformity in the terms of sale, or rental in this case. Second in the service offered in the course of the transaction and any follow-ups there may be, and third in any subsequent service performed. This --what I had here -- was written in connection with goods rather than money and the reference here is to repairs and the furnishing of spare parts, etc. There is no exactly comparable thing in the case of money, it's simply the service -- whatever service and accommodations are involved, the collecting of what is owed, and that may perhaps involve the extension of some leniency in the event of failure to meet the terms of the loan.

Securities are an example of perfect

uniformity, my notes read here, such as a common share of CPR or of Nickel. Now it seems to me to be equally true of money. The question of the terms of sale, the service offered both in arranging the loan and in the collection are another matter. This would be true even though the rate of interest was identical in both transactions that were being compared. There is, that is to say, some differentiation in lending apart from the amount and the rate of interest which distinguishes one lender from another and reduces somewhat the perfectness of the market. I'm not arguing that this is a bad thing, it's probably well that some lenders should be nicer to deal with than others, more accommodating in the event of failure. It's too much to ask, I think, that they would all be perfectly delightful to deal with or wholly lenient when the debtor falls down.

Fourth, there must be perfect knowledge in a perfect market. Buyers and sellers must have adequate knowledge of market conditions, supply and demand, current prices and there must usually be some organization to this end. Now we are concerned here with, I think, a much more rudimentary thing. The money itself is known. It's rather the price at which the money is available and I suppose also some knowledge of the terms. It should be possible for the price to be known according to some formula, as I mentioned at the outset. It is harder to know the terms of the sale but if standard terms are provided that knowledge becomes unnecessary, at any rate so long as you know

about the type of transaction you don't have to have special knowledge when you enter into a transaction any more than you have to have special knowledge when you buy a pint of milk. You know what a pint is and once you know that you know what's necessary.

As to the service offered in negotiating a loan and in taking the payments subsequently, it seems much more difficult to have perfect knowledge as between lenders A, B, and C -- they can only be known by repute. Extreme cases, of course, can I suppose be taken care of by the Better Business Bureau. I don't know whether the Better Business Bureau offers information in this field, but if they don't it is quite conceivable that they should. And if a borrower wants to know whether the business reputation as to the man on dealing and collecting for a particular firm is satisfactory, his knowledge would be more perfect if he could find out through the Better Business Bureau. He might perhaps find that someone was offering money at very much less than others and he might begin to wonder if there was a catch in this -- are these people particularly hard in collecting? What is the gimmick in this? And if he could get that information from the Better Business Bureau or someone else, then his perfect knowledge in this field would be made more or less perfect.

Various types of organizations have existed in markets to make knowledge more perfect, and one necessarily talks in terms of commodity markets

rather than money markets as a rule in this, and I think I need only refer to things that are commonly recognized. In the organized markets one of the first forms of organization to make more perfect knowledge is arrangements within the Exchange itself for the recording of transactions. You know in buying wheat or shares of a company, you know what the transactions have been in previous days and you can find out at the end of the day what the transactions have been on the day in question, the various prices at which transactions have been closed.

Second there are arrangements for rapid and preferably instantaneous communication between trading centres available to all who are prepared to pay for the service of telegraph or ticker, or if you are willing to wait you can find that information in the newspaper.

Finally a certain amount of statistical information is usually provided, indeed always provided, in a perfectly organized commodity market. Now how far you can by analogy seek the same arrangements in markets for consumer credit I don't know, but I simply put this down as an academic requirement and a technical requirement for a perfect market. If these things are lacking to a greater or lesser extent, then knowledge will not be perfect as it could otherwise have been and the borrower, and of course at times the lender, will be at some disadvantage in making his choices.

The fifth condition of a perfect market

is -- I think this follows from what was said at the outset -- absence of discrimination. This is a point which is not always emphasized because as I said, it seems to be eliminated automatically if there are a great number of buyers and sellers. But Professor Kenneth Bolling, whose discussions of the conditions of the market have attracted a good deal of attention emphasizes this point that the buyer and seller must be willing to enter the transaction with all and sundry. In business affairs this means that there shall be no special discounts, no special agents, no under the table arrangements. The whole thing shall be above board and universal as to the manner in which the transaction is carried out.

Now those are the things which I regard as most important for a perfectly competitive market. I think this could be elaborated on but I am not prepared to do it today and I don't know for our purposes we need go any farther than as far as I have gone here. Anyone who wants to look at the development of markets over a period of time will find that histories of commerce and markets are helpful in showing how one characteristic after another of a perfect market has appeared with the development and improvement of commerce and transportation and so forth. I find in my notes which I used ten or fifteen years ago in lecturing to large classes of beginners in economics, that a volume by Vernon A. Mund entitled Open Markets provided a fairly good historical survey of the development of markets concerned mainly with

markets in produce rather than markets in money, however.

Now the position of lenders who advocate a hands-off policy rests, insofar as it can be defended in the eyes of an economist, rests on the view that markets in consumer credit are perfect, or very nearly so. And the conditions that I have mentioned here are the ones --the first ones at any rate -- that have to be examined if one is trying to decide whether that assumption of virtual perfection of the market is justified by the facts.

I have heard defences on a number of occasions given by representatives of the consumers finance industry -- that might not be quite the way you describe it, but I think you know what I am referring to -- I'm not entirely a newcomer to the argument that they offer. It's perfectly clear to me that the terms on which loans are offered don't on the face of them give the cost as an interest rate to the consumer. From time to time I have put aside the tables that are published of the amount of payments for a certain loan -- I have quite a collection of these, in fact -- and rarely if ever do they state an interest rate. They simply show the number of payments to be made over six months or a year or two years in order to finance and discharge a loan of X dollars.

So one of the first conditions for perfect knowledge appears to be lacking as far as the consumer or borrower is concerned. Indeed, it may well be that this is the principal lack in the -- when one is

judging the degree of perfection in the market. After all there is nothing, as I said earlier, that is more uniform than money itself. You don't have the problem that you have in connection with potatoes or strawberries that one package is different from another package. One hundred dollars is the same as another hundred dollars, and one of the greatest difficulties in many fields, other than the standard commodities like wheat and so on which are traded by specialists, is completely absent. Now that's a great point for a perfect market. That money is standard. Furthermore money can be moved from place to place at exceedingly low cost. Lack of availability and cost of transport is not a problem wherever there is a banking system and the banking system in this country covers virtually the whole country.

MR. IRWIN: I think maybe -- he is having trouble transcribing with your hands in front of the microphone.

MR. MacGREGOR: Oh, I'm very sorry. There may be some places in the far north where owing to the lack of banking arrangements it is not easy to get money transferred, but I think that is a very small qualification.

Two of the conditions then of a perfect market are met as ideally as anyone could hope for in connection with lending. Uniformity of the product and the ease of movement of it. And it is rather a -- there must be a very serious impediment to the perfectness of the market in other fields if, in

fact, the behavior in the market seems to be that of imperfection. That is, one where there may be what appears to be irrational or ill-informed transactions taking place.

The second characteristic of a free market which is lacking for perfect knowledge, the second thing which is lacking is the limit of time horizon of borrowers. This is something which is peculiar to the borrowing of money. Ordinarily the time horizon is not a factor in people's purchases, transactions, except in the purchase of highly durable things where people may lack a knowledge or interest in their long term durability. Not to imply that it is wholly confined to money, but the number of transactions, the proportion of transactions, where consideration of time, of extending it to years, enters is not very great. But there are some, of course, where the time consideration is far more important than it is with loans -- the purchase of a house, for example. A person who is unable to think in terms of what time, in the sense of five or ten or twenty years, may do to a house will be a poorer judge of a house than a person who can envisage what time will do to it.

I'm not competent to say how far people are skilled as buyers of real estate, but I would point out if he has any doubt in his own judgment he can easily engage for a rather small fee an expert appraiser who will tell him what the house is worth and what the prospects are as a long term proposition. The situation is rather different, however,

because the amount of money involved in the transaction of a house is so much larger than the normal consumer loan that it would justify the high rate of a specialist to give you a specialist's advice, whereas most consumer loans are -- I don't know what the average value is, average amount is -- it depends on the type of loan. But I suppose in automobile deals the average amount would be rather less than a thousand dollars -- would that be correct? Something of that order, roughly half the purchase price of the car, allowing for your cash and your turn-in? It's small, at any rate, in comparison with the cost of a house and hence the incurring of the expense for professional advice is less justified. I am not aware that one can get advice on consumer loans other than by going to the Better Business Bureau. If it were available and available on terms that people could afford to pay, it would probably contribute somewhat to the perfection of the market.

There seems to be a peculiar quirk to the time horizon of the public in borrowing money. People are willing to pay a very high rate for money which they borrow whereas they do not ever expect to get, or at any rate never succeed in getting and I don't suppose many of them expect to get, comparable rates for money they lend. That is to say, a person will put money in the bank for 3 or 4% in a savings account voluntarily and not complain that he has been ill treated while he will think nothing of paying 15, 20 or even 25% on a time payment arrangement. And he

will probably continue to keep his money in the savings bank. That, of course, seems quite irrational, but after all they serve a function. The money in the savings bank is there as a rainy day reserve and the interest involved is after all quite secondary. That may be why this discrepancy appears -- between the price which people are willing to pay and the price which people are willing to take on the market. It isn't after all -- without further other information -- it doesn't seem rational. If they are willing to pay 25% for the use of something and only to be asking 4 or 5 when you are offering someone else the use of it. Surely the rational thing to do would be to take the money on which you are getting 4 or 5% and put it all into reducing the purchase on which you are paying 20 or 25. Now there are doubtless some people that do that. But I am suggesting there are others that do not. I think their reasons are sensible ones, but this is an element on the time horizon which is, -- I must confess, it rather puzzles me,--I don't feel that I am able to account for financially, or convincingly as I should.

I encountered this, Mr. Chairman, some years ago in connection with an inquiry into pensions, with which I am connected -- I am a member of the Ontario Committee on Portable Pensions and had something to do with drafting their principal report -- and here we were faced with pension plans which were giving people $3\frac{1}{2}$ or 4% on their money and the same people were going out and obviously borrowing at rates of 15 to 25%.

There was, in the case of the pension plan, some evidence that people were avoiding having their money tied up because the majority of people, whever they got an opportunity to unwind the whole affair, did so; but at considerable loss to themselves. I am referring to cash withdrawals on the part of a person who, when he changes jobs, gives up his membership and takes out the money he has put in. That, of course, applies to a contributory plan. He takes out the money that he has put in and he gets a refund of all his own contributions, sometimes without interest. But when he does that he also foregoes whatever the employer has contributed. And in almost every case the employer has contributed indeed. The Dominion Government's definition of a pension plan includes a contribution by the employer. The individual who takes a refund of his contribution foregoes the employer's part in it which may be quite a large amount and gets his money back. He can use that money to avoid paying 25% on time payments, of course, pay cash for a car. Or he can put up more money for a house, whatever it may be. Nobody knows just how money which is taken back in this way is used, but from the point of view of personnel officers that were interviewed by the Portable Pension Committee, the money was not used for particularly constructive purposes. That's something you may have heard about. We found that there was some quite detailed information on this taking back of money by way of refunds in the case of the Dominion Government Pension Plan where the actuaries in their reports give a table

showing the proportion of people with five years or more of service who on leaving the Dominion Government will take a refund. The proportion is high and it continues high until late in life. I have a table here which gives that information. Even on into their late fifties a surprisingly large proportion of them withdraw their own contribution and forego the Dominion Government's contribution. The young man may not forego much, but a man in his fifties who has five years or more of service foregoes a great deal, usually more than his own contribution.

THE CHAIRMAN: What would be the alternative to withdrawing the money?

MR. MacGREGOR: The alternative would be to leave the money there and to get a pension at the age of 65. He wouldn't lose anything, he would just have to wait for it. But waiting is irksome for most people. People don't like to wait. And that is the next point in what I have to say, that the future is uncertain. People may not live to be able to enjoy the future. Chances that they won't live are, mathematically speaking, of course very small until one reaches an advanced age. But the possibility that one may not be alive and the greater possibility that one may be either not living or infirm, which is a greater possibility than simply death alone, is an argument for enjoying now -- buying now and borrowing if necessary.

There is another aspect of this , of the uncertain future, which I think one has to remember,

that quite apart from death and the possiblity of infirmity, life is a very frustrating experience and there are all manner of things which make it impossible time and again to do the things that one wants to do. So and so has fallen ill and it costs money or it has taken time and attention. So and so in the family has to be at school or has to be on the job. So and so is visiting the family and there is a social obligation. And there are obligations to voluntary organizations and the rest. Anyone who has been in a family of any size knows how difficult it is to get all the family together for as much as half a day with all the commitments that various members have, quite apart from the question of cost. This is what I mean when I say life is a frustrating experience. I mean frustrating for anybody who has a project he wants to carry out. You want everybody to go away for a short holiday together, or a motor trip. You want them all for a social event or you want them all in, say, to enjoy a new motor boat or something of that kind. Unless they can all be there or nearly all of them the project isn't worth while.

When every now and then the future does seem to open up perfectly clear and there are none of these obstacles, I suggest that people are at the point where they are more inclined to have a fling. And as these opportunities sometimes develop rather rarely, the question of the cost of having a fling is a bit secondary. I don't know whether this has anything to do with the psychology of consumer borrowing, but I think

it may be an ingredient in it. I know in my own experience there have been times when I have undertaken an expense, sometimes at what might seem an excessive cost, simply because it was the opportunity that presented itself. There wasn't time to consider or prepare, the thing was to get it over with while you were able to, by next year it might be out of the question.

Two years ago my wife went to Europe on very short notice and by methods that certainly were not the cheapest because it seems all the circumstances made it possible to do. And this summer I did some building at my summer place. It wasn't the cheapest. I could certainly have done it more cheaply if I had looked around. But all the circumstances made it possible for me to undertake the work at this time and the possiblity of being able to use it quickly opened up and I decided to go ahead. And undoubtedly I paid rather more for it, but on the other hand, I had the thing when I wanted it. In other words, urgent demands arising out of opportunity may make people pay more than they would otherwise, may lead them to undertake what might seem to be irrational transactions but which when you look at the whole situation in the light of that person's own reckoning, are probably satisfactory.

The next item as to an absence of characteristic of a free market is one that I mentioned already, credit terms not being easily comparable, and I needn't go into that again.

Those, it seems to me, are the principles of a free market that are lacking and the task I suppose of gentlemen in your position is to decide whether the absence of these characteristics in whole or in part so impairs the market as to justify some intervention in it.

At this point I would distinguish between two types of intervention. There is what might be described as negative intervention, which simply says "Thou shalt not charge this" or "Thou shalt not enter into a contract of such and such a duration" or "Thou shalt not lend unless there is a certain amount of downpayment". The other type of intervention might be described as positive intervention and it seeks to improve the perfection of the market by declaring a rate of interest or by some other device seeks to make good the deficiencies that I mentioned a few moments ago. I think it would be correct, Mr. Chairman, to say that on the whole economists favour positive intervention in dealing with imperfect markets rather than negative. It is well known that they favour, in the case of the labour market, measures to improve the mobility of labour, which is a positive thing. And on the whole measures of that kind have, I think, justified themselves. I needn't go into that, but just to refer to the measures by which you develop an organized market in labour with communications between one section and another, preferably on a national basis and such a market exists, to some extent, under the Unemployment Insurance Commission. And in addition you

train labour by adapting your educational system to the needs of the labour market and you make efforts at retraining labour later in life. So these things are all receiving a great deal of attention just now because of the effect of automation. But these are positive measures and I would prefer in the field in which you are interested that you should come up with recommendations that included positive as well as negative measures. There are, for one thing, a good many more positive measures that may be chosen from than negative measures.

I have raised the question in my notes here as to whether consumer lending agencies are sufficiently specialized and sufficiently numerous in the various specialties. This question was implied in an earlier remark and I think that in following the logic of the methods that I have been following, an answer to that question is necessary and it should not be too hard an answer to secure. The question of how much dearer consumer credit is in Canada than it is in the United States seems to be worth attempting. Money is dearer generally speaking in this country than in the United States and there are well known differentials between the two countries in other fields and I would suppose that if the consumer credit market in Canada were organized with about the same degree of effectiveness, the spread between Canadian and American rates would be a fairly uniform spread and would bear some sensible relation to the spread between, say, between bond rates and mortgage rates.

Now, Mr. Chairman, perhaps I had better go back to my list of questions and see how far -- whether there is anything else.

Your second question as to whether the legislation might provide limitations in respect to downpayments -- I would think that perhaps there ought to be some limitation in respect to downpayments. I realize that competition tends to reduce the downpayment to something approaching zero. It would seem to me that it must result in a rise in the number of repossessions, particularly in the more durable articles because it gives the individual a chance to abuse the service that is extended to him. I'm thinking more in terms of houses than other things but I suppose it applies to other things.

And as to the standard forms of contracts -- if possible -- I don't feel that I am qualified to -- without knowing how many forms of contracts, standard forms, let us say, within certain areas, may be possible -- but how many types of contracts are required for different types of transactions I am not able to say.

Now as to economic effects of legislation which would have the effect of reducing the amount of consumer credit, of consumers borrowing -- it seems to me that there is a step in the reasoning here which is taken in one leap. It is conceivable that a more perfect market in consumer credit far from reducing the amount of credit to consumers might increase

it. If there were a more perfect market, if people had confidence, knew better what they were faced with, more confidence in the terms, more confidence in the fairness -- and one might go so far as to say in the integrity of the operations -- that there would be more rather than less borrowing. It might not perhaps be by the same people. It is possible that people who do not borrow, they are very careful to avoid it, would enter. I've never borrowed in terms of consumer credit that I am aware of. I might if the terms were known to me and also a little more reasonable.

Now when we suggest that the effect of intervention might reduce the amount of borrowing, as I say, we are conducting a piece of reasoning, the nature of which has not been disclosed. We are jumping to a conclusion. What I have just suggested it is not the only consequence. But we must assume, for the purpose of this question, that the consequence of some control or some intervention -- I don't like to use the word control because that implies the negative type of thing -- but if the consequence of some intervention is to reduce the amount of borrowing, then what would be the consequence? It has been suggested, Mr. Irwin wrote, that the economic effects might take the form of a decline in credit buying with implications of a reduction in employment and economic expansion. This is a hardy old argument that consumer credit is maintaining the economy, keeping up the level of employment output and making us all richer, in a

collective sense. But for this there would be less output and naturally fewer durable goods around. Perhaps even less travel because nowadays I believe you can travel now and pay later.

Well I don't take that argument very seriously. I'm speaking as one individual who has to do with economics. If the effects of intervention, which in turn is here assumed leads to less borrowing, are introduced gradually, I think the economy could accommodate itself to a smaller amount of consumer credit without any serious dislocation, especially if some compensating arrangements were made as they ought to be in the field of banking. It is the purpose of the central bank to, so to effect the banking system as to absorb changes of this kind. An expression that was here a good many years ago in The Economist -- a case if not for the featherbed, at least for shock absorbers. It's not the business of a central bank to be a featherbed, but it is the business of the bank to provide shock absorbers and this can be done through the interest rate and the open market policies of the bank. Its influence is not all pervasive, of course. If it were felt that a greater amount of shock absorbing was necessary the national budget would be the other place where adjustment would be desirable, some reduction in taxation that might not be considered as necessary, might be a useful form of shock absorber.

I am here thinking of a rather drastic change in the amount of credit buying. But if the change

were smaller and came about by degrees then measures on this large scale and measures on this scale might not be -- a shock absorbing scale -- might not be necessary.

I realize that this is not something on which all people will agree with me. The thing that bothers me about the answer I have given is that -- summed up, or alluded to at any rate very compactly in the expression incentive goods -- it's widely recognized, I believe nowadays, that the ability to buy certain types of goods provides an incentive to people to work and to save or repay, which is another form of savings.

These goods have to be first of all obtainable. During the war they weren't obtainable. And people who might otherwise have been working very hard knew that they couldn't buy automobiles or refrigerators or washers or radios or anything of that kind, were more inclined to take it easy than they were subsequently when these goods were obtainable. First of all then the goods must be obtainable in a physical sense -- that goes without saying -- or that particular incentive to work is lacking.

Now how far the ability to obtain these goods a little sooner, due to consumer credit, is a further ingredient in the incentive -- I don't know. That is the point at which I worry about the position I take here. If,in the judgement of people who are as well informed as it is possible to be on any matter, the facility which enables people to get these incentive

goods a year earlier than otherwise or two years earlier than otherwise -- that is to say without having to save up in advance -- if that is a noticeable ingredient in the incentive then the withdrawal of part of the credit facilities would only mean that fewer of these goods -- that these goods would be less available to the public, in fact and in its own estimation; and if they are less available, then some people will work less and other people will save less as a result. This is a thing about which I don't feel at all certain -- it's, I think, the weak spot in the position that I have just taken. I'm not able to evalutate it, but I admit there is that weakness there. I find it hard to understand myself, the fact that something can be had by saving for a year without any of the inconvenience or danger of borrowing, will greatly deter people, but I am told by those who have to do with this that that is their opinion. That is, I suppose, one of the things that you have to form an estimate on.

I would emphasize that again and again there is the importance of certain types of goods as incentives to effort, have come to my attention and it seems to be an element of human psychology that is not included in the ordinary discussion of the market of demand and supply. It doesn't occupy any noticeable place in economics but it does seem to occupy a place of some importance in the real world. It was during the war particularly, when these goods were not available, that consumer credit was secondary,

they simply were not available, that the absence of these things began to be appreciated as an element in the economic scene. I remember that my late colleague, Professor MacGregor Dawson, who did a report on economic conditions in Nova Scotia at that time -- he and a number of other people -- found that among the miners the income tax was having a noticeable effect on the miners in discouraging them from doing overtime work, but it was not only the income tax -- his view was that the absence of goods of this type, which were becoming available just then and had been becoming available just then to them and were improving their lot considerably, upgrading their houses. The absence of goods of this type, he thought, was an important factor as well as the income tax in leading these men to quit work after a standard working day, even though it was very much desired that they should work longer hours.

Now the next item on the list: The economic effects might take the form of transfer of cost of borrowing to the price of the article. I have to confess that I don't quite understand what that question is directed to, nor even quite what it means. Does it mean, Mr. Chairman, by transfer of the cost of borrowing that the article might be quoted at a higher price all around, including the cost of borrowing, whether it was paid for in cash or by time payments?

MR. IRWIN: Mr. Chairman, could I help Mr. MacGregor in interpreting my own question? One of the suggestions that has been made before this

Committee by lenders, particularly lenders under conditional sales contracts, is that if intervention, as you so easily put it, occurs and that intervention took the form of particularly requiring the lender under a conditional sales contract to declare to the borrower the rate of interest which he is being asked to pay, that as an attempt on the part of the lender to reduce the rate he will be obliged to quote, that he would reduce the finance charges and recover that cost by increasing the price of the article sold. And the lender, to advance this argument, seems to imply that this would be a wicked thing and against the public interest, so the question is directed to get an objective evaluation from yourself, as an economist, as to (a) would this likely take place and (b) is it a bad thing?

MR. MacGREGOR: Well, as I said before, I pay cash and I would dislike it if I felt that I had to pay an enhanced price which included concealed interest because of an arrangement of this kind. The question would seem to be: Is there any way that I can avoid it by seeking another dealer, any way that I can avoid this enhanced price? And at that point the question arises: How many dealers are there? Now if there are a large number of dealers I would hope that some of them would find it to their advantage to quote a price which didn't include any loading for finance charges that in fact were not involved. The dealer might call himself a discount dealer -- I don't call what he calls himself -- but I would hope that I

could find a dealer who didn't load his prices this way. If there were enough dealers I would feel pretty sure that I could. It becomes a question of the extent of competition among the dealers.

Now there are some cases, I suppose, where the number of dealers is very small or where the number of ultimate suppliers, in the case of motor cars, is very small and where, even though there is a law against resale price maintenance, there may be a good deal of cooperation, and it might be that I would have to look very hard and perhaps look in vain for a dealer who would give me a price net of this loading. I think that's all I can say, gentlemen. I think this is a point where the degree of competition may be a very important element in the answer.

MR. IRWIN: In other words, if the market could be made as perfect as possible perhaps with the assistance of government intervention, that this occurrence might not occur?

MR. MacGREGOR: I would think not. But I'm suggesting here that it may not be the lending --not perfection in lending but rather perfection in producing that would be the determining factor. It's very much harder, I think, in production, which calls for enormou sly large scale operations nowadays to have a perfect market than it is in a matter such as lending where as far as I know there is no very great economy in large scale. We are involved here, you see, in the manufacturing end rather than in the lending and financial end, it seems to me. And I think it is

going to be much, much harder to get the perfection one might hope for.

MR. IRWIN: Except -- I don't want to start asking questions at this time -- but would not the effective point of competition be at the retail level, not the manufacturing level?

MR. MacGREGOR: Well, in the eyes of the law, yes, if you have a law against resale price making. The question then becomes whether even with such a law there is an element of de facto price making, something that can't be deported in law but in fact exists. I don't know whether that's so. I really don't know what the effects of our law against resale price making is in practice. It would turn very largely on that. One would hope that retailing on the whole is a pretty competitive business, that I would be able to go to someone else, but if it's in the automobile field -- I just wonder. I have no information.

MR. IRWIN: Because of the existence of the franchised dealer my observation would be that in the new car field, dealing with the big three franchises, I think what you say, there may be a certain amount of de facto price making, but in regard to, say, appliances, this would not hold true.

MR. MacGREGOR: I see. It's a good thing there are quite a number of suppliers of appliances. I have been worried a little lately about proposals that have been coming in from all sides that there are far too many producers in Canada of this and

that and the other thing. These people seem to be advocating or leaning toward a wave of consolidation such as we have never had before in Canada. I'm afraid if that came about we would find the same thing in washers and soaps that we find in automobiles. Then they say: "Oh well, you have a very low tariff and these things will compete with foreign production." It is the same thing that is going on in foreign countries, and if the tariff ceases to be low we would find ourselves skinned right and left, but I'm afraid I'm getting off the subject.

MR. EDWARDS: Mr. Chairman, don't you think these problems would resolve themselves if there was some way to arrive at what is a fair profit?

MR. WHICHER: You won't get Mr. Reilly's support on that. That's a queer question for a druggist to ask. (Laughter)

MR. MacGREGOR: Well, if I may participate, I have heard of businesses that charge very high prices but didn't make any profit.

MR. MACDONALD: Mr. Chairman, I had the feeling both yesterday and today that this question is a bit of (inaudible) -- to this extent: I don't think the problem is that you are going to reduce the profits of a credit agreement and raise the price of the product. The reverse is the problem that I think we are faced with and I would be curious on this particular point to have your assessment as an economist. Namely, there has been a tendency to reduce the price of the article and to recover the losses there or the lack of

profit there in your credit operation. The tendency is to go to the point that you can't even buy it for cash, and that is really putting you in a spot -- you and I apparently operate on the basis of not using the consumer credit field very much -- but what would your comments be on the economic implications on that tnedency? Because even where they don't refuse to sell for cash they conceive the same end by pressuring and slick presentations and that sort of thing so that they end up by suckering the consumer into buying at a lower price on credit.

MR. WHICHER: Did you say you never had to borrow?

MR. MACDONALD: I said I never bought anything on credit.

MR. WHICHER: Get that in the paper. (Laughter). We are finally getting to know you.

MR. MacGREGOR: They have access to the more perfect knowledge. They have sources from a high --

MR. WHICHER: I think that's right.

MR. MACDONALD: I'd like your comments rather than --

MR. IRWIN: Besides the knowledge you have got to have the money.

MR. MACDONALD: Are there any serious implications in the false reduction of retail prices and recovery in the credit cost?

MR. MacGREGOR: Well, sometimes when you go into a restaurant that has a licence you find

the meal is surprisingly cheap but if you add to the meal some liquid you will find at that point you are no longer in the same price bracket. (Laughter)

Now in the case of the restaurant, particularly if you come in with guests, you are under some social compulsion to buy on the upper scale of prices as well as the lower. Whether you are under the same social compulsion to borrow money rather than to pay cash I doubt very much. I think there is some analogy between the two things, there is what you call a rock bottom price and then an extra service at a much higher one. If the dealer can count on getting enough of the high prices or more profitable business it will compensate him for offering the low prices.

MR. MACDONALD: In other words, if you had a more perfect market so that the consumer knew what he was paying for credit, this tendency of burying the profits in the credit would end very quickly?

MR. MacGREGOR: I think it would. I find it hard to see that there is any compulsion in a thing of this kind, for people to tend to use the credit if they have the money. There is certainly not the social compulsion that you have in your banks. If they knew what they were paying I think you are correct. I think it might prove a rather nice example of what would happen if you did introduce the conditions for a more perfect market you would find that people use their common sense as soon as they are able to apply

it. There may be cases, of course, of cajolery and there may be, too, -- I have a hundred dollars, let's say, to spend and here is an article for a hundred dollars. But the merchant may take this line: "Now there is another article that goes with this, the washer and the dryer. Now here's the washer. You can have the washer for $300.00. But how much better it would be to have the washer and the dryer. Now you have got $300.00 and you can have the dryer too if you are willing to enter into a credit arrangement. I'll take your $300.00 and you can get credit for the rest." Where one purchase leads to another I can imagine a good salesman convincing a person that he might as well take the second purchase now and borrow.

I think that this transfer of costs, as I suggested earlier, the transfer of costs of borrowing to the price of the article is something that is likely to occur mainly where there is a degree of monopolistic power. Now when I say degree of monopolistic power I mean it as a much qualified one, but it's something that every businessman would like to possess if he could -- that's only common sense -- and a good many of them venture a little way with it and succeed. It's a matter of how much competition there is and how much potential competition there is whether you will attempt to hide the price of your article. I think that's all one can say.

If the manufacturer behind the scene has very little influence on the price at which goods

are sold at retail then I would think that this would be a comparatively rare occurrence. But it's a big "if".

Now the next item in this -- I will read the first sentence just to bring it back to you -- it has been suggested that the economic effects might take the form of (a), (b) -- now we come to (c) -- realignment within the lending industry -- that is to say, more borrowing from institutional lenders and less from private lenders.

Well, it's obvious that realignment is continuously taking place, going, going,going on all the time and if the institutional lenders provide money on better terms than the private lenders and if the public has the means of knowing what the terms are, I would expect there would be. Not everyone in the public is a fool as to his own advantage. And if you can get for 10% at the banks what you would pay 15 or 20% for elsewhere and if the banks terms are satisfactory -- that's an important element -- I would expect people to go to the banks. I don't know whether you had in mind anyone other than the banks in using the word "institutional lender".

MR. IRWIN: If I could just assist you again, having written the letter, Mr. MacGregor. One of the -- or another,in this case implied rather than stated, submissions by lenders before the Committee is that if there did occur some intervention as you describe it and particularly in regard to disclosure of the rate, that this might well cause a

dislocation of present lending practices taken as a broad spectrum, where you have, for example, on one end, the extreme end, what you might call the fanatic lender on second mortgages on poor property who is charging rather exorbitant or apparently exorbitant rates of interest of 40, 50 or 60%. You also have certain well known institutions in the sales finance field who are charging in the area of 15, 18%. And you also have a number of people in that area who have set up private companies of their own and are maybe getting 20, 25%. And so on. In every field of lending in the spectrum there is what you might call the recognizable institutional lender and then in that same area of the spectrum there are sort of other private lenders who are operating in the same field. The suggestion is made that the tendency would be by intervention to eliminate the sort of minor private institutions in favour of the well recognized public institutions -- not just banks or not just insurance companies, but recognized sales finance companies.

MR. MacGREGOR: I see. It would have a tendency, perhaps, to drive out the small private institution as opposed to the publicly known institutions?

That puts a sharper edge on the question. I think that would depend partly on the legal position enjoyed by the small lenders who presumably are lending to the higher risk cases. I think they are able to work their way into the suppliers in this market because

they are prepared to buy credit on somewhat different terms, on more generous terms, at any rate, as the borrower sees it superficially, than others. Certainly less cautious. They are rather like the person who is willing to buy a third or fourth mortgage which no trust company is likely to do.

I do wonder whether you could ever eliminate these people, except by fiat, because there will always be borrowers who are more anxious than the average borrower to have the money and who are in a weak position as far as credit worthiness goes, and if there is somebody who is willing to take a chance and engage in that rather finicky and at times distressing, perhaps rather nauseating business, it's rather like the pawn shop business, isn't it? I wouldn't expect that they would be eliminated altogether. I would think that the realignment would rather be between the big boys until they were brought more to a level. That would be -- just off the top of my mind -- that would be my impression.

Now if you alter the legal position, if you make it more difficult to recover, if loans are made under very risky terms, with less than a specified amount of downpayment, something of that kind; then I would think that the number of people who are willing to enter this field would be very much reduced. I don't know whether it is desirable or even possible within the ordinary principles of the law to introduce it. The question as to how much support the law gives

to incautious lending is, I think, a matter of some importance.

If the law on one hand gives support to incautious lending and if on the other hand there is an Unconscionable Transactions Act, you might very well say whether the law is contradictory or not. The question would arise as to whether it is a consistent position for the state to take.

On the one hand it may be a contra-cidtion between the common law and statute law which is a little easier to envisage.

MR. IRWIN: Could I just -- I'm not so much asking a question as helping you to answer the question, Professor MacGregor. As an economist and following along the lines of your own thinking, as the -- if the market were made more perfect by intervention, would you expect that, even amongst the institutions or the publicly recognized lenders that would increase their competition and have some effect on the average rate?

MR. MacGREGOR: I would think so, I would think so. That answer implies that people at the present time are unable, because of lack of knowledge, to patronize the organizations that can provide money at the lower rates. That if they knew they would divert their patronage from organizations which from one defect or another are unable to quote low rates, divert their business from one to another; and that would, on a weighted average, undoubtedly give a lower overall average. You would have to have a

weighted average in order to achieve that, but that's what you have in mind there.

Now there is back of that answer a doubt, or rather reservation, which I said a little earlier, that you may bring into the community of borrowers new borrowers as a result of your intervention. I suggest that I might be borrowing. There may be borrowers of the substandard kind who would conceivably be brought in also. But they would still probably show some response to the better information available to them. But I was thinking perhaps rather more of the fringe, that there may be other people who are now beyond the fringe who, if they felt that this was a safe thing to do and it was well supervised by society, would come in and be at the fringe. And at the fringe the costs are high. Here I'm thinking of the fringe in your average. I just want a footnote on that.

I think you have to be prepared quite unexpected responses to what you have done that might on the surface appear to disprove or invalidate your judgment, but your judgments are ordinarily formed on certain assumptions that you are dealing with the people who are now in the market. A lot of new people will come in who have suddenly become confident that this is all right. Then you are dealing with almost a different world. That is something that could happen. I just warn you that things might not work out quite the way you or I would expect.

I wouldn't see any particular harm in

it, no. The whole thing would probably reach another equilibrium after some adjustments, both in the field of the borrowers and the field of the lenders there would be an equilibrium established after the intervention takes place.

It is possible that the lenders too might be different under a new system, a system with intervention; with more confidence people who regarded it as beneath them to be in the field would feel that it has now become a comparatively respectable field. You might have quite a different supply situation. I think you might perhaps find an analogy in the vending of alcoholic beverages as a result of government intervention in that field. There were a lot of people who run cocktail bars who wouldn't touch the thing in the days of the tariff, but a cocktail bar is fairly orderly and moderately respectable undertaking in the days when liquor was vended through taverns, they wouldn't be involved in it at all. You have a different supply situation when you have a more orderly and to a degree a more perfect -- I wouldn't want to suggest that the vending of liquor is a perfect market because of restrictions and so forth -- but it is more respected with the standardization of the thing.

I think you would have to envisage a very considerable change right across the board. It makes it harder to anticipate the total result, but I don't think that the additional and more remote consequences one needs to be afraid of. If they were

something to be afriad of, they I think the whole inquiry would be very much more difficult.

Now there is here (d) the reaction of business and (e) the reaction of the public. I doubt, gentlemen, whether I can say anything that you couldn't say more effectively with more knowledge than I could as to how business or the public might respond to intervention if it were intervention that were carefully applied, with some regard to the views of business before it was applied -- I wouldn't expect any very unfavourable reaction. Is this being reported to the press, what is being said here today?

THE CHAIRMAN: Yes.

MR. MacGREGOR: Then I think perhaps I better not say what I was going to say. (Laughter) What I would say is, if business is given an opportunity to express its views, not just on one but on a number of occasions as legislation developed, forces of panic or objection may be allayed. Partly by making business more aware of what is proposed and partly by modifying the proposal itself.

MR. IRWIN: Further to that question, Professor MacGregor, would you care to comment in this regard -- I'm sure you must have other analogies to draw from -- that when intervention takes place on the part of government by the imposition of a new tax or the raising of a tax or a form to be filed, etc., etc., the tendency of the business community -- and this is what I am asking you to comment on -- would be to accommodate itself to it and then go on having accepted

and oriented to the intervention, whatever it was. How would you feel about that? Would this be a valid suggestion?

MR. MacGREGOR: Well, it is true that that is what the business community does but, if you think of the tax example which is a very good one because of the very great amount of experience in that field over a long time -- when you think of the tax example it immediately draws attention to the number of unexpected consequences of intervention. It's true that business does somehow accommodate itself. Sometimes by the failure of businesses that can't make a go under the situation, sometimes by various forms of cutting and trimming. The individual business may be well enough satisfied when finally it comes to a new equilibrium but when you look over the whole state of the thing from the standpoint of society, the new arrangement may be very much inferior to the old one. This can result. Then you come to the question of weighing the unsatisfactory elements against whatever advantages there are in having the tax revenue, the things that the government has been able to pay for with this money that it couldn't before. So you have a series of detriments on one end of the scale and a series of advantages on the other end of the scale and you try somehow to estimate the comparative parts of the detriments and the advantages and you come up in favour of what has been done or against it.

Now, of course, that is only the first

comparison. The other comparison is the particular thing of intervention or the tax that has been employed as against some other tax arrangement that might have been employed. Then you are weighing the comparatives of one scheme of taxation as against another scheme of taxation. You may or may not decide that the thing that was done was the best under the circumstances.

There are any number of examples of taxes that have led to rather unexpected consequences which may not have been of much concern to the business people involved, but were of concern to the whole society. We don't have the conspicuous, easily explained examples of these (inaudible) -- they lie a century or more ago. Nowadays we have more sophisticated examples of the same thing but they are much harder to explain, such as income taxes and profit taxes, the untoward effects of these are rather abstract and hard to discover by statistical means, but there is a good deal of reason to believe they are there. The conspicuous examples are the kind that you got a long while ago. An example that I use in lecturing to my students -- because I give lectures on the subject -- is drawn from the taxation of the State of Denmark some three to four hundreds of years ago. It was customary to put a tax on vessels that passed through the Baltic Sea into the North Sea around the Sound. It is a narrow channel, only a couple of miles wide, an ideal place for levying a tax on shipping. But there was some delay in getting

the shipping through and raising the tax, and so they devise a simple way of measuring the ships for the duty. They took the length of the ship and the width of the ship halfway between the bow and the stern, multiplied them together and the tax was based on the product.

Well the Dutch were building most of these ships and they were very skillful shipbuilders and in a very short time the Dutch were producing a ship that was shaped like an hourglass. They had a very narrow beam and so the tax was reduced. Well the hourglass ship didn't last very long. When it was discovered the Dutch were as clever as the Danes they changed their formula. But this led to a lot of rather expensive if not too substantial shipbuilding.

You can have unexpected consequences in the product and sometimes in the technology and so on, which I can't go into here. You have to be on the lookout for those things.

As I say, on the matter of reaction on the part of business and the public, of course you threw it back to me on this more technical field, but that would be my answer to that particular question. There are some.

Now as to the reaction of the public, I am not quite sure what you had in mind there except that they might disapprove of the party in power that did this. It has made it harder to get things on time.

MR. IRWIN: I think I can help you there by saying that you have really answered this

question in several comments. The reaction of the public for example -- if a development of more perfect competition might possibly attract people like yourself who have not been in this market, this would be one reaction of the public. Also possibly it could be a reaction of the public if, as a result of more perfect competition, there was a withdrawal of supplies on one hand at the fringe and a withdrawal of borrowers at the fringe. This would be a reaction of the public. I was just wondering if you had any others. In other words, would there be more buyers, fewer buyers, different kinds of buyers? Would they understand generally what was going on? Would it be confusing? One of the things that has been suggested here is that intervention in the form of requiring a rate disclosure would be confusing to the public and that this would discourage them from using credit facilities. What would be your reaction to that?

MR. MacGREGOR: Well, I would think that the people who feel confused would probably ignore the information. They would have a crack at it and find that this was above them and go on in very much the same way they do today. But the others would look at the information -- not at first, it would take them a while, I think, to size up the new situation -- but by degrees people and their friends would between them get the sort of knowledge that is required. People don't act alone in these things. They talk to one another and read things about it and by

degrees they acquire a certain amount of knowledge. That's what I would expect. Certainly you couldn't expect immediate results.

I think there would be quite a bit of rearranging, a kind of musical chairs, how this thing is going to come out. There would be quite a little rearrangement and one would expect that undoubtedly it would be to the advantage of the public. Some people would stay out of it. Some people would suddenly discover what it was costing them and they would prefer to save the money. I think that would be true. Others would prefer to pay -- people who are urgent purchasers and borrowers of the type I described -- now would know what they were paying and some of the more exaggerated rumors would cease. There is evidently quite a bit of exaggerated notion of what things costs among the public in a number of fields. I think it would allay that. So you have movements in and movements out, and to some extent in the whole situation it cancels out.

Now I don't think that means that nothing is accomplished. I think that people who come in and are satisfied where formerly they weren't and people who are out are probably happier to be out. I would think the general happiness would be increased and the confidence and sense of integrity of the business.

MR. IRWIN: That's what I had in mind.

MR. MacGREGOR: I would think that

MR. WHICHER: In your opinion, Professor, there should be a rate disclosure?

MR. MacGREGOR: I think it would be desirable. I think this thing was put very neatly in another field by Mr. Douglas-Hume when he spoke of (inaudible)

MR. WHITE: Mr. Chairman, may I dwell on this point for a minute? You used the term rate disclosure, but earlier in the conversation that was taking place we talked about the revelation of the cost of credit. And the point that perplexes me the most and I think many of my colleagues are likewise in doubt, revolves around the nature of the disclosure. Should that be, in your opinion, in absolute dollar cost coupled with a term or period of time or should it be a rate of interest using one standard method? Now the representatives of the business community who have attended here have almost been unanimous that they would much prefer this disclosure in absolute dollar amounts. They have argued that it would be more meaningful to the average buyer, that it would be much simpler for their employees to calculate and so on. I have been sort of brainwashed by Professor (   ) and certain other economists who have written on this subject and who feel fairly strongly about disclosure as an annual interest rate and when these various witnesses came before us I was one of those who asked searching questions. I still haven't made a decision in my own mind. I'm not sure. I would like to draw a couple

of points to your attention and perhaps get your views on them.

First of all there is quite a lot of doubt in the minds of our legal advisors whether we can encompass all lending institutions in legislation as provincial. So it may be that chartered banks and similar institutions will be excluded. And I think I am right in making that remark, am I not?

MR. SEDGWICK: That is right.

MR. WHITE: Secondly, we know of at least one form of credit, namely revolving charge accounts, where this standard method could not be applied, for reasons that I will not go into.

So here are two sources of inequity. If we do attempt to impose a rate of interest calculation I am disturbed a little by the complaint made by businessmen that it will interfere, that it will impede some legitimate business transactions. For instance if one is selling a tractor to a farmer in a field and the contract is written on the fender of a car, then the calculation of the interest rate, while it may be fairly simple using tables in an office, does become complicated and I can imagine him postponing and in some instances eliminating that transaction.

The money market is a fairly good one, I think, relative to some product markets and I am wondering if limitations placed on these financial transactions in a relatively small jurisdiction

here in North America might frighten capital out of the Province. It's not as if we could legislate for the whole continent, in which case the effect might be quite different.

MR. MacGREGOR: Well, on the last point first. The only capital which could be frightened would be the capital in the hands of private individuals who make use of consumer credit. A farmer who might be thinking conceivably of moving from New Brunswick to Ontario might be dissuaded, conceivably, by this. But I can't see how the sort of capital that we ordinarily think of today being concerned at all about consumer credit unless it is in that business itself. That may be what you had in mind. That finance companies in the United States or conceivably Great Britain that might have entered the Ontario field and by so doing might have rendered the market more perfect, might be dissuaded by the Ontario legislation from doing so if they didn't like the legislation. That may be what you had in mind. I think that is a possibility, assuming that the effects of the legislation were unbalanced. I suggested that they might not necessarily be unbalanced. But assuming they were I should think that might be a possible consequence. Whether that is a consequence of enough importance to weigh in this Committee's consideration I wouldn't know. As I said earlier I am not able to say how competitive the supply is in the various compartments of consumer credit. But beyond the dealers in consumer credit I wouldn't

think it would be important enough to merit any thought whatever. Individuals don't come to Ontario because of the availability of consumer credit. Corporations who come to Ontario don't use consumer credit. They might, of course, be dealing in a product where consumer credit was a factor in merchandising and if something were done in this Province that made the merchandising very different from any other part of North America, I could imagine that a manufacturer in the United States who was thinking of opening up in Canada would not do so, at any rate not in Ontario. The financing of the sale of his goods would be greatly impeded. But I can't imagine that the Province of Ontario would introduce legislation of that kind.

What would hurt the impending American enterprise would hurt the enterprises that are already here. I can't imagine that you would favour anything that would be so detrimental as to do that.

MR. WHITE: Well I judge from your remarks that you have a fairly strong opinion that disclosure of the cost of credit using some kind of uniform formula would improve the market, increase efficiency and add to the general well-being. Am I right?

MR. MacGREGOR: Yes. I believe so. I should add that I am not at all sure that it is fair to require that the whole cost be expressed as a rate of interest because it is clear that the cost

of much of this type of credit is a combination of a rate of interest and a service or administration charge. The sum of these things can be expressed, if the charge is a proportionate charge, as a flat rate. But if the charge, the service charge, is not a proportionate charge, then the larger the amount of the loan the smaller the rate which is involved. It seems to me that if they want to head off the charge that they are engaging in usury that they should be allowed to state that so much is interest and so much is a service charge, or collection charge. That might be a flat sum or it might be a graduated or proportionate sum. I would suppose that the service charge ought to diminish in proportion to the loan. As the loan rises. Because it doesn't cost any more to collect 20 payments on a loan of $2,000.00 than it does to collect 20 payments on a loan of $1,000.00. As far as I am aware it involves the same operation, the same man hours, the same paperwork.

MR. WHITE: Do you think that the cost expressed in dollar terms would be a reasonable way to start universal disclosure of cost of credit here in the Province or do you think the Committee should consider a more radical solution, that is, the revelation in an interest rate?

MR. MacGREGOR: I think this is a case where I would not be against revelation. I would be all for revelation.

MR. WHITE: We all want revelation, but

do you want it in a dollar amount or --

MR. MacGREGOR: Oh, well, by revelation I mean in percentage. Yes, I think people are entitled to see this recorded as a percent. If you want to see it quoted so much percent interest and so much percent service charge, all right, but I think it aids the public. Just as it is reasonable when you are giving the people information on the goods they are buying at the grocery store, that they should be able to be presented in a form that they can make use of it to their own advantage.

MR. MACDONALD: Well, to go back to your basic principle that it is desirable to have as true knowledge as possible, unless you put it in an interest rate you don't have full knowledge for shopping purposes. A person is incapable of calculating all of the variables --

MR. WHITE: He doesn't have to do that though. The only difference is this: If you express a rate of interest and you have one figure, you have an annual rate of interest, all this information compressed into one absolute amount, whereas if you are expressing the cost in dollars you have to couple that with the term. That would be right, wouldn't it? All right. Now then, I'm going to fall back on a principle of Professor MacGregor's, that he mentioned earlier as a personal belief of his -- when he said that if changes were introduced gradually the economy could adjust to a lessening in the total amount of consumer credit

available and that is one of the reasons I put this question to you, sir. It seemed to me that you might favour revelation in dollar amounts initially and if that didn't work perhaps a little more radical solution by requiring the revelation of the cost of credit in the form of an annual interest rate.

MR. MacGREGOR: Oh well, this organization of merchandising nowadays has been so carefully designed to take advantage of human psychology along selling lines, impulse buying and prestige appeal, all manner of things, that it seems to me that you ought to try and give some help to the individual who wants to exercise his intuition in his favour, as well. The biggest load is against the poor guy now. He can only exercise his intuition to buy and not to be cautioned. If you can provide him with information in a predigested form which will enable him to exercise his intuition in his own interest as well. I think you are only regressing the balance. It seems to me that the balance is already much disturbed by scientific merchandising.

MR. WHITE: But what is your objection to revealing the cost in a dollar amount?

MR. MacGREGOR: I have no objection to that, only that's not enough. You should be able to get this as a percentage as well.

MR. WHITE: What's the advantage of having it as a percentage?

MR. MacGREGOR: Because one knows that 5 or 6% is a modest rate of interest for most purposes

--5 to 7%, 7% being the common rate for borrowing on houses. And if this rate is 20% then it is not a modest rate and a noticeable ingredient in proportion. Now it's true it may be only a few dollars but that is where much of this business has been built, and it is not in absolute terms a large sum, but nevertheless I think people are entitled to have this proportionate amount. If they get accustomed to this thing because they bought something on time that cost $50.00 where the actual burden on their pocket was small, the next thing you know they will be buying something for $200.00 and then it will be $500.00 -- by that time they have gotten into bigger figures, they have been nursed along. I think they ought to know the price of the nursing.

MR. WHICHER: Professor, I suppose you are aware that in other jurisdictions in Canada large business ventures that are doing business in Ontario now disclose it as an interest rate. We had that example yesterday when Mr. White wasn't here. I think most of us were amazed that the T. Eaton Company in their revolving accounts charge 1½% of the balance at the end of the previous month. Now I think it is a fair question if they are willing to do it there, because there is no compulsion, why wouldn't they do it here? I think that's maybe a question that Mr. White should answer instead of yourself.

MR. MACDONALD: Mr. Chairman, I would like to go back to Mr. White's question, regretting that he wasn't here yesterday, while he will

have a very good brief that he can read and capture most of what he missed. We are sorry you missed it for this reason. I think of the reservations that have grown up in your mind, they are greater in your mind than they are in mine although they have grown up to some degree in my mind, were pretty well resolved yesterday by Ziegel. For example, to take the two that you raised, namely that you can only cover part of the field and you can't cover banking. Ziegel conceded this, but I think his conclusion was that that is not an inhibition to doing what you can do within the field over which you have jurisdiction. In fact it may well act as a catalyst in forcing, particularly at this present time when the Banking Act is coming up for review next year, that the federal government will complete the job by action there.

Secondly, as far as I am concerned, while it doesn't achieve a perfect result, even some of the serious reservations I had accepted from Mr. Irwin on the revolving account, have been somewhat minimized and even discovering that Eaton's in other jurisdictions are operating on 1½% on the balance of the previous month.

MR. WHITE: That's a different matter.

MR. MACDONALD: I agree it's a different matter, but I'm hoping you won't be averse to reverting to your original brainwashed condition. (Laughter)

MR. WHITE: Well now, may I just clarify

one other point? You indicated, Professor MacGregor, that you were in favour of setting a minimum down-payment. Is that an economic point of view or a social one?

MR. MacGREGOR: Well I would say both. I think a vendor, a lender, ought to -- each of the vendor and lender ought to exercise reasonable prudence with whom they do business. And if failure to exercise prudence, in the absence of some sort of intervention, a proportion of them fail to exercise reasonable prudence and enter into transactions, the completion of which is going to involve something that could be termed unconscionable, then some form of intervention is desirable to reduce this entry into transactions of that kind. A specified down-payment is one way of doing it.

It seems to me the people, for example, who go out and buy a house with a $500.00 downpayment are entering into a transaction that may have very undesirable consequences for both of them. This is very common and it is found in practice that the results are unsatisfactory, then something in the way of total downpayment should be considered.

MR. WHITE: There have been alternative suggestions on this point, one of them being that the collateral for the loan be restricted to the goods actually purchased at the time and that other household things possessed by the buyer not be joined in in some kind of a chattel mortgage. And also that after a certain percentage of the loan has been paid, three-

quarters or 80% or some such figure -- that the goods purchased not be repossessable. Now it seems to me that solutions like that provide the answer to the social problem without having the same economic consequences as establishing a minimum downpayment, which I think might (inaudible)

MR. MacGREGOR: I haven't given any thought to that alternative. I doubt just off the top of my mind whether it really is a clear alternative. It seems to me you are dealing with rather different situations. I look upon a downpayment as a means of exluding a certain proportion of people whose ability to carry out the transaction is very doubtful. As in other matters having to do with price, it is a very effective and impersonal way of excluding a certain amount which for one reason or another is better not exercised.

There may be certain exceptions to this but I would have thought that they could be dealt with by other means. The provisions of downpayments, money, by some form of assistance coming from outside, may at times be desirable. I think that's an alternative face of it that might be considered. You can undoubtedly point to hardship cases because of the downpayment that is required. But there are other ways of dealing with hardships than by relaxing the terms on which a transaction should be made. I would prefer to consider those other ways before I went to no downpayment.

MR. ROWE: The effect on the

economy of the no downpayment can be possibly studied because there was a downpayment required back in 1940, I think as low as a third, as I recall. If this had an effect on the economy I do not recall.

I was involved in a credit business at the time and I know it affected me very directly and drastically.

MR. MACDONALD: Well, wasn't that the deliberate objective at the time?

MR. ROWE: I just mention it because it isn't a new idea to require downpayment and the effect of this action can be discouraging.

MR. MacGREGOR: I wouldn't think that a very noticeable change should be made abruptly unless you have some other reasons. Now when you get into a war or a foreign exchange crisis you may have some overriding reasons for wanting to discourgage demand and this is one way of doing it. Britain has had fluctuating terms of hire-purchase in recent years, but unless you have one of these reasons at stake, clearly the change from a 5% downpayment to a 25% downpayment ought to be made in steps.

MR. WHICHER: The matter of this interest rate, Mr. Chairman, being able to say what it is in revolving accounts; Mr. Rowe was talking there and he is a stock broker and I was wondering about the margin account. I believe it is about 6½% interest that you charge?

MR. ROWE: 6-3/4.

MR. WHICHER: 6-3/4, all right. Well,

do you charge that on a daily balance?

MR. ROWE: Yes.

MR. WHICHER: On a daily balance.

MR. ROWE: Of course the balance changes quite frequently during the month.

MR. WHICHER: Yes, that's right. I was comparing that to the revolving account, say, at Eaton's. Does that make a great deal of extra work for you?

MR. ROWE: I can't answer that. I would think that it would, but I've never been in that --

MR. WHICHER: Nevertheless you do it anyway.

MR. MACDONALD: There is less and less work with modern machines.

MR. ROWE: Oh, yes. Now it's all worked out with an IBM machine.

MR. IRWIN: I think this is the point I was making yesterday -- is it a brokerage office?

MR. ROWE: Yes.

MR. IRWIN: Well, brokerage offices are now right in the field of using computers, not only for transactions but for calculations and with the advent of their use it has become perfectly easy to make these daily calculations. It is just until that time arrives it is a rather onerous matter in the case of the department stores.

MR. LAWRENCE: Department stores are using it?

MR. IRWIN: No, not quite yet in the context we are talking about, evaluating the daily balance and calculating a rate per day on that balance, they haven't got to that stage yet, but they will do that.

MR. WHICHER: That's why Eaton's charge 1½% in Saskatchewan on the balance, instead of on the daily balance. If that's how they do it in Saskatchewan why couldn't they do it in Ontario?

MR. IRWIN: I'm not disagreeing with you, I'm just saying to do it on a daily balance you need a computer to do it.

MR. SEDGWICK: I think they do it here but don't announce it in the document.

MR. MACDONALD: Mr. Chairman, while we have the benefit of an economist with us here, there is an aspect of this that I would like to raise. It seems pretty fundamental in the light of the consideration of what we are charged to do in this Committee. Implicit in the questions of Mr. White and a good deal of Professor MacGregor's testimony was that intervention in this field would result in a reduction in the amount of credit and therefore have a serious impact on the economy. I must say the more I listen to the arguments, I think this is a completely false assumption. I think that if you have large perfection of knowledge you will find there are people today who, because of a lack of knowledge, getting credit at 25 or 27% will get it at 15 or 18 and will have that much more money available for

consumption and therefore it will result in boosting the economy rather than reducing it.

Secondly, there has been some emphasis -- perhaps not too consistent as yet -- where other Provinces, other jurisdictions have intervened in either a negative or positive fashion, that it hasn't, by testimony of the businessmen involved, it hasn't reduced their sales -- other factors compensate for it.

And you have the third factor -- I suspect this is a pretty big one -- of old fashioned people like ourselves who haven't used this, and alternatively people in various degrees who have a lack of confidence -- that if it were regularized it would be a benefit to everybody concerned and you wouldn't find less credit, you would find more credit, or far more would use effectively their credit because it would be used at 15% instead of 25% that is being frittered away uneconomically in this field rather than being used to keep the wheels of industry going.

Now this, I think, is a pretty fundamental background consideration for what we are charged to do in this Committee and unless I am very wrong in the conclusion I am coming to, it's about time we quit dealing with false assumptions to what might be happening when, in fact, the evidence leads to the conclusion that the alternative would be the case.

MR. REILLY: Mr. MacDonald, don't you

think you and the Professor are in the few class rather than the many class? There are so many people who can't afford not to use the facilities of credit. Most people, on the contrary, have to use it if they are going to purchase things. If you and the Professor are able to pay cash for it I don't think it's indicative of most people.

MR. MACDONALD: Well, I don't want to get into a personal argument about this, but all I say is the answer to the question is No because it is part of the Victorian, if you will, background --

MR. WHICHER: The Scotch background. (Laughter)

MR. MACDONALD: Also a Presbyterian background. And here is another point that is relevant and this is a good time to bring it in, which I was quite fascinated by. We live in a very contradictory society and economy today; we pay lip service to these old values of thrift and savings and things of this nature, where it is, in fact, the whole fact of the economy from the approach of the credit unions and the approach of advertising -- Buy now and pay later -- so that we pay lip service to principles which are completely invalidated and aren't being followed.

One of the other interesting points that Professor MacGregor brought up was that to buy on time creates an incentive for hard work because if you are committed to paying for something that you have got -- you have got (a) the satisfaction of using

it, (b) and you have got the compulsion -- you know the damn bill is coming at the end of the month and if you don't pay it you are going to get into difficulties. And this may be an incentive to harder work. Now this is a very interesting reversion from the Victorian approach. In fact the amount of purchasing that is being done on time is an incentive to more work. You are driven by the very fact that you have to work to be able to pay for it.

One thing I would like to find out from Professor MacGregor, Mr. Chairman. Basically where is the urge for a percentage disclosure rather than a dollar disclosure when most people pay for things with dollars rather than on the basis of percentage? Only from the standpoint of money borrowed for mortgage purposes or large investments of that nature dealing with money do we think of it in terms of percent. But the average person spending money today, earning money daily, getting paid on a salary basis of weekly basis in dollars, knowing what it is going to cost him to buy something on the basis of dollars, where does he learn disclosure, on what basis -- percent? Certainly not for the general public. It should be our job to assist the public to be able to get a more perfect market.

MR. WHICHER: I think the urge is by the T. Eaton Company. They do it without compulsion, in many jurisdictions of Canada.

MR. LAWRENCE: We had evidence

presented to us that there are large sections of the public that say (rest inaudible)

MR. MACDONALD: The Canadian Association of Consumers, which has studied this field presumably has at least evoked a conscious reaction on the part of the consumers that they are very unqualified in this.

MR. LAWRENCE: We hear that every year by a number of large associations.

MR. REILLY: Oh, no, I don't think so at all. On the contrary I think this body is sitting because of the situation that has developed where people have been rooked, where there has been flagrant abuses, and that wasn't necessarily on the basis of percent, it was on the basis of dollars.

MR. LAWRENCE: A lack of an opportunity for them to compare.

MR. MacGREGOR: I think it may be said, Mr. Chairman, that first of all a great proportion of the Canadian public has had some training in school in reckoning interest. Virtually everyone nowadays has had to for a year or two, so that they know what interest is. And second a noticeable proportion of the public now owns Canada Savings Bonds. Now a Canada Savings Bond is the best form of collateral and I think if one owns one or two or more hundreds of dollars worth of Canada Savings Bonds one is in a position to borrow from a bank. And the bank will loan it to you for 6%, they may loan it to you for less, if you have Canada Savings Bonds as

collateral. And if you have a head on your shoulders -- and mind you I'm not certain, Mr. Reilly, that everyone has a head on their shoulders. Certainly not as good a one as Mr. Reilly has -- but there are a good many people who do have a good enough head on their shoulders to use what they learn in school and compare, if they have the information, the rate it will cost them at the bank and the rate which is given them by some other lending organization. If they can get them. The suggestion that this should be kept in an incomparable form it seems to me is putting up a barrier for them which they may find very hard to overcome.

MR. REILLY: One other question, Professor MacGregor, in connection with the downpayment. Do you have in mind a downpayment should be used regardless of the amount being purchased? I can understand, for instance, the reason for a downpayment on a home, but I have the feeling you suggest a downpayment should be used for any amount -- a hundred dollars? Twenty-five dollars? Or five thousand dollars?

MR. MacGREGOR: Well, I think your pencil has a good sharp point on it, Mr. Reilly. Certainly there are small things where the person is trusted with no downpayment required if the person is known to the merchant. You buy something for $25.00, let's say, I would doubt whether the requirement of a downpayment on as small an amount as that would be necessary. It is expected, of course,

that you will pay the whole sum at once or in two or three -- you are not, in other words, contemplating an instalment arrangement at all. But if there is to be an instalment arrangement it would seem to me that a downpayment, possibly a graduated one, but some payment for the smallest transaction on which an instalment arrangement was provided, would be desirable. Just to maintain the principle of the thing, but it is surely not acceptable from that standpoint, not as an important matter. If there is a $50.00 transaction -- I suppose there are time payments on $50.00 transactions --

MR. ROWE: A lot of times these $50.00 transactions are added on to an existing account and the downpayment really loses its meaning. The total unpaid balance is probably no larger than the original amount.

MR. MacGREGOR: Well, if it means it is mounting up that much higher when there is already something there, I suppose that would be an argument perhaps for a larger downpayment, rather than a smaller one. But my answer to Mr. Reilly's question would be that if there is a hire-purchase transaction, a hire-purchase agreement, that even on small amounts a downpayment is desirable. You could argue that. I'm not going to express an opinion, but you could argue whether the downpayment should be larger. There is also the question of a minimum below which the transaction would not be allowed at all -- negative intervention. I think this

might well be considered.

MR. KERR: Professor, aren't we really getting into two different spheres here? The idea of making sure that the public, the consumer, is aware of the cost of goods, of the percentage terms of the loan and even the cost that he is buying. We also should do something to control or regulate or intervene in the hard sell type of selling. Then when you get into the business of downpayments, controlling downpayments, then you are a form of prohibition here. Don't you think that this would have more detrimental effect on the economy than the other types that I have mentioned?

MR. MacGREGOR: Yes, I think so. As I said earlier, the positive type of intervention is preferable to the negative type. But I suggested just a moment ago in connection with Mr. Reilly, that this might be a case where the negative type might have to be considered.

MR. KERR: You made the remark that you shouldn't buy a house with $500.00 down. There are hundreds and hundreds of people in my area buying homes, $12,000.00, $13,000.00 homes with $500.00 down. It seems to be difficult today to save $500.00. Now these people might be young people in the acquiring stage of life, they have a certain amount of confidence that they will improve their station in life as they become older. They are able, as a result of knowing the terms of the contract or agreement for sale or something, what the contract is going to mean

to them, what committments they have. They are responsible people, they plan their budget, you might say, to buy a home, or whether it is a refrigerator or even a car. We shouldn't prevent these people from doing these things. As long as they are aware of what it is going to cost them.

MR. MacGREGOR: Well, it may be that you are running against a personal purchase based upon experience in this field, because this is the one field of lending where I have personal experience. It may be that it's not altogether representative, but just to support your own argument let me make my own for a moment. I think this can be said, that next to Canada Savings Bonds and similar securities, a house is the best security that I know of for credit transactions. But it is the nature of mortgage credit that it is inflexible, particularly where there are more than one mortgage, and also it is expected to negotiate and to adjust. It can be argued -- this is your type of case -- it can be argued that when people are setting up a household they should borrow as much as they can on a house, if they are going to buy a house. In order to avoid getting into these more expensive types of borrowing, that can be argued. The more so as having once borrowed on a house it is not as easy to borrow more even though you may have a noticeable equity in it. You committments in the early stages of housekeeping are going to be heavy for a variety of reasons and it is better to concentrate

your borrowing in a field where rates are rather low and the security is accepted -- that's the case for your position. And when you look at the whole situation and not simply at the situation as seen by the mortgage lender, your position becomes stronger. I expressed a dislike of small downpayments, I expressed it mainly from my experience with mortgage lenders, and from my knowledge of what conservative lenders prefer. When the whole situation is looked at, I repeat, the argument is a stronger one. If, however, the young people who buy a house on $500.00 down and then go out and buy all these other things on time at 25%, then they have got themsevles, of course into an exceedingly weak position. They have not taken advantage of the one form of borrowing to release them from the other. They can get into an awfully hopeless condition.

MR. KERR: I am thinking, Professor, only of the, as I say, using a little bit of caution and individual responsibility here. They shouldn't buy a home, a bigger home or more than they need. In other words if they are raising a family and they can't find an apartment, for example, they will buy a small bungalow. They should realize that they can only afford so much. This is where they put the $500.00 down. I agree they should certainly be aware and take some precaution of the interest rate, the total cost of borrowing. Other things that they are acquiring -- for example they need a stove and they need a refrigerator, things like this that are essential,

really, rather than a luxury today in a home, this is the type of planning they should do. And certainly they should wait, for example, they may have to use an orange crate instead of a chair or something like that for a while. I was just worrying about -- you seemed to imply that they shouldn't even be in that position. They should be prohibited by some form of regulation or control of being able to take advantage of this type of goods or merchandise or asset.

MR. MacGREGOR: I wonder what the experience of the lender is in situations of this kind? The prudent mortgage lender sees it this way, as I understand it. That if he lends on a house purchase where the downpayment is trivial he is in great danger of having that house thrown back on him at the end of the first 12 or 18 months. Because the purchaser of the house may find that he can give up his interest in the house and be better off than if he had been renting a house in the meantime. That is the ordinary view of the mortgage lender. I have with me here something that came in this morning's mail, calculations done by a well-known firm in Boston on a not very large loan, as these things now go, of $10,900.00. Now let's suppose that this house had been sold for $500.00 more than that -- $11,400.00 -- actually there was a much bigger equity than that, but let's just suppose for illustration. This was a $10,900.00 loan, 7%, $105.00 monthly. I may say this is a renewal of a loan, consolidation of a first and second and when

renewing this I insisted that the payments be made as much as it had been before under the first and second. Otherwise it would have been probably a flat $100.00 -- the loan had already run five years when it was renewed.

Now the question -- the reason I raise this is this: How much comes off that $10,900 in the first 12 months? And the answer is $525.00 in the first 12 months. Now suppose the $500.00 had been paid down. The person who threw up this house at the end of 12 months would lose his $500.00 down and his $525.00 off principal, assuming that there was nothing left in the event that the house was sold. $10,025.00 for 12 months, which is about $95.00 a month -- something of that sort -- no, less than $90.00, under $90.00 a month -- between $85.00 and $90.00 a month. That man will have been able to have a house between $85 and $90.00 a month. This is a nine room house, by the way. He wouldn't have got a nine room house for $11,400.00 -- let's say a six room house. And he has had this house, which would have cost him to rent -- what, $110,$120.00? Perhaps more than that.

MR. KERR: The interest on that, though, is the --

MR. MacGREGOR: Well, he will have paid the interest as well, that is correct. He will have paid $1,260.00 altogether, you are quite correct. He will have paid $1,260.00 for the use of that house for a year and he will have put in $500.00, $1,760.00.

So it is about the equivalent of $150.00 a month. It's a little hard to see -- on the other hand, his loss will be very small compared with what he would have paid had he rented a house of the same size. And the question now arises, what about the prudent lender? How is the situation like this arise if lenders are prudent? Unless borrowers are more creditworthy than they used to be. Because this kind of thing of throwing up houses used to happen rather frequently. My experience with this goes back to the time when I was quite young, back about 40 years and it used to be quite a problem. Whether people are more reliable than they once were, whether with various forms of security, financial security now afforded them then are less likely to get into difficulties and are reliable for that reason rather than because of character, I can't say.

MR. ROWE: Don't you think possibly because of the labour market that with young couples both of them are working, they have more money to --

MR. MacGREGOR: That could be an important element in it. They have two incomes rather than one and that is quite commonly, probably more often than not the case today. At any rate for a while until the children arrive.

MR. EDWARDS: Then they should have more than the $500.00 to pay down?

MR. MacGREGOR: I think this is a very appropriate observation.

MR. WHICHER: In my mind anyway Mr.

MacDonald is wrong -- there is no argument in what he calls the two opposing forces in our economy. To me they are all going to the same point because this, for these young couples, not only a major form of savings for them -- at least in Southern Ontario at any rate -- they appreciate in value. Not only is it a major form of savings it is the only major form a savings. We would be treading very dangerous ground to get into this field at all as far as restrictions are concerned.

MR. LAWRENCE: Well, you can get credit under the National Housing Act, you are lending under Central Mortgage and Housing. There is no problem to buy a $13,000.00 home with $500.00 down, particularly with working bonuses and all these sort of things. But these people, of course, do get a credit check on the borrower. A person to qualify on a loan of this size is pretty well scrutinized and the lender assumes there won't be any default. In the case you are mentioning I think this was more a private arrangement where the builder is selling a home on $500.00 down and taking an agreement for sale. It is nothing more -- the buyer there is nothing more than a glorified tenant really. The $500.00 is really a few month's rent in advance and this is a situation where we are more worried about the lender here.

MR. MACDONALD: Mr. Chairman, are we coming back this afternoon if we have further questions?

THE CHAIRMAN: Yes, we are coming back anyway to hear Mr. Irwin. It's just a matter of if it is convenient for Professor MacGregor to come back.

MR. MacGREGOR: I have a committment at three o'clock, Mr. Chairman. But I could, if you wish, come back for about 45 minutes.

Mr. Chairman, might I be given the opportunity to read a paragraph of written matter here that bears on the immediately preceding discussion?

The argument that people in an "affluent society" -- I put quote marks around that expression which was introduced by a well-known writer recently -- the argument that people in an affluent society can easily afford credit can be reversed. People who are so well off can save more and should either dispense with credit on all but house and possibly auto purchase or at least make much larger downpayments. Many of them too should get their small loans from the bank on collateral in Canada Savings Bonds or other sound security.

To the extent that people are today better protected by insurance against loss from mishaps, including death, their creditworthiness should be greater than otherwise, other things being the same. The question arises whether such people are actually able to get credit on easy terms, say 6 or 7% and by what route.

There are reason for believing that

there is a type of person who almost habitually and with pride in his capacity to do so tries to squeeze through the cracks of the financial business and legal and tax systems. He moves without leaving a forwarding address, changes jobs often, lives common law, deserts his family, drives an uninsured car, collects a surprising amount of unemployment insurance, etc., etc. Now there are not very many people who have all of these guilts to their credit, but you know the few that I am getting at.

No doubt he borrows if he can and is hard to collect from. The questions arise: (1) how successful are the central service organizations or credit organizations patronized by the lending companies in identifying people of this type? (2) in the case of a young person who has recently entered employment how long does it usually take to identify those who become one of these poor rists? And are the defences against them raised soon enough?

Considerable publicity is given to overall statistics of the ratio of consumer debt (usually excluding mortgage debt) to consumer income? That has a bearing on the question of overborrowing by weak or other borrowers. Unless it is broken down to show the proportion of people with above average and below average debt and who they are, this ratio between totals may be very misleading. Even a fall in the overall ratio of debt to income could be accompanied by a worsening of the situation.

That's all.

MR. MACDONALD: I have a question that flows out of that. There are a minority of people who just simply cannot handle credit. They get into trouble and you pull them out of it and they get back into it fairly quickly.

Now our problem at this level, the legislative level, is to what extent is it legitimate to intervene positively, to protect these people. We have done it, say, with alcohol and other aspects of society. To what extent is it, in your view, legitimate to intervene in protecting this small minority and what are the economic dangers involved? The broader economic implications of what inevitably is going to be a blanket law and can be applied to everybody rather than being applied to only a small minority?

MR. WHICHER: How small would that minority be? I think we should know that before you can answer that question.

MR. MACDONALD: Well for the moment I don't know. For the purposes of getting an answer I don't know that we need to know that.

MR. LAWRENCE: Maybe we could get an estimate from the Better Business Bureau.

MR. MacGREGOR: There is information available on the repossessions and back payments, but that doesn't tell you whether these repossessions are from the same people repeatedly or over the whole market at random.

MR. LAWRENCE: Coming to Mr. MacDonald's

question, the last part of the question points to the problem. If these are a small proportion of the whole and I suppose they are, it is hardly an economic problem in the ordinary sense of the word. But intervention that is designed to deal with something quite small may grow, may be extended beyond the field for which it was intended and may be regarded as a precedent perhaps for further intervention. And at that point it becomes of interest to the economist who is concerned about the extent and character of this intervention.

My own inclination in dealing with situations of this kind would be to examine the extent to which imprudent lenders get support from the Courts, or any other form of legal support. Whether they perhaps get too much support in imprudent lending. I don't know but I would wonder. I am astonished at the imprudence of some of the lending one hears about. This is just something I know about from the newspapers. A year or two ago there was a report on garnishees of employees in default. Some employee at City Hall had had his wages garnisheed in a matter of a year or two some 45 or 50 times. Finally he was fired. But some official at the City Hall had become quite concerned at the amount of work that was going on in the pay office because of the garnishees of employees' wages and these statistics were compiled.

Now, some of these people have been getting credit and it would seem to me that prudent

lenders wouldn't be lending to them. Is there imperfect information or are the lenders so automatic that they don't seek information? I don't know the circumstances under which a man with 44 garnishees to his name gets a loan and results in a 45 garnishee. But I must say I raise an eyebrow when I hear that such things can arise. I don't feel particularly sorry for the guy who has been able to outwit the lenders in this case, unless he loses his job. And at that point I think perhaps a little bit more prudence on the part of lenders might be good for him.

It's important to note that there too this man was trading on the fact that he was an employee of the government.

MR. MacGREGOR: I would suppose so, yes. Evidently they take that as meaning something.

MR. LAWRENCE: I wanted to ask a question -- I apologize if you have covered it and if so, say so, and I will read it in the transcript. I was late coming in to ask a question on non-recourse paper.

MR. MacGREGOR: Would you explain to me what that is? I don't understand the technology of it.

MR. LAWRENCE: Well I gather it is the sale of a negotiable instrument which in some manner or other prevents the original vendor or owner of the property from going back to the person who now holds the note. I gather that there are two

markets in the sale of commercial paper today -- one dealing with non-recourse paper and the other with ordinary negotiable paper.

MR. MacGREGOR: That question hasn't been raised and it is not a case on which I could express an opinion on.

MR. SEDGWICK: Professor Ziegel dealt with it --

MR. MacGREGOR: It's not an economic question.

MR. SEDGWICK: No.

MR. MacGREGOR: I'm not familiar with it. I would have to look at it to say, and I really don't know anything about it. Most of the things I have said today are things about which I have had some occasion to think at some time or another, or had some experience with or some observation.

MR. MACDONALD: I think positive intervention in this field would eliminate some of the fly-by-night operators.

MR. BUKATOR: And lenders.

MR. MACDONALD: Well, operators in terms of a man who puts siding on a house and sells the paper and then the homeowner discovers it is inadequate and he has no recourse, he can't do anything about it. I think you would get rid of the joker who is skipping from Owen Sound to Timmins to Brampton --

MR. BUKATOR: Just one minute, Mr. Chairman, if you don't mind. I don't want to miss this opportunity. You are going to have awful time

moving me away from that percentage rate revelation. I'm more convinced than ever after listening to Professor MacGregor.

I originally was one of the very few who thought this was a proper procedure and I thank you for your comments.

THE CHAIRMAN: Would you care to make some comment on a cooling off period?

MR. MacGREGOR: I would say that it appeals to me, if only that a (rest inaudible) I would have thought that it wouldn't do any harm and it might eliminate a certain number of imprudent transactions. Whether this is something that should be extended to the lender as well as the borrower is something I have wondered about.

THE CHAIRMAN: We never did get into that. Any way of getting rid of door-to-door salesmen I would agree with completely.

MR. SEDGWICK: The questions I had in mind have been mostly covered, but I just wanted to come back to our agenda so that I could reduce your evidence to the narrow avenue of my understanding. And I take it that as to the first question,that is, the feasibility of calculating and expressing the cost to the borrower in terms of a rate percent, you completely agree with the evidence that was given to us yesterday and with the brief that Mr. Irwin has prepared, that it is quite feasible providing we settle on a standard method of computation -- that is the only --

MR. MacGREGOR: I believe that is so. I have talked to colleagues of mine who deal with insurance mathematics and they are actually involved in interest calculations and from my conversations with them I gather that while there are differences, acceptance of one standard rate enables most of the necessary comparisons.

MR. SEDGWICK: Yes. And that really answers the second part of the question, the economic implications, on balance you think it would be desirable that the rate which the borrower pays should be expressed in terms of a percentage. And you give a very good example. When he deposits his money in the bank he gets 3%. If he decides to borrow money he should know whether he is paying 3 or 30%.

As to the next (d) as to providing limitations in respect to downpayments, I take you are somewhat ambivalent. You are inclined to think it is desirable and you agree with what Mr. Kerr said, that you wouldn't want to say so as a general rule. You certainly wouldn't want to fix them in terms of a percentage of the amount borrowed?

MR. MacGREGOR: No, I think not, I think not. This is a field in which I haven't done what some people call heavy thinking on this matter, but I would agree on --

MR. SEDGWICK: Yes, and then as to the rest of the agenda, that is the right of repossession, the cooling off period, permitting the

borrow to retract, which is a phase of it, standard forms of contract, etc., would it be fair to say that they are not economic but legal problems that did not really fall within the purview of your study?

MR. MacGREGOR: That was why I left them out of my remarks. I didn't feel that they were especially pertinent to the questions that I was brought here to answer.

THE CHAIRMAN: Well, as Professor MacGregor said earlier, he is getting quite attached to being aroun d here and on behalf of the Committee I would like to say we do appreciate your being here this morning to give us the benefit of your advice. I am sure it will be very helpful to the Committee.

Gentlemen, we will meet here this afternoon at two o'clock.

---WHEREUPON THE MEETING ADJOURNED UNTIL 2:00 P.M.

---UPON RESUMING AT 2:00 P.M.

THE CHAIRMAN: Mr. Irwin is going to speak about some of the matters which deal with disclosure of interest rate.

MR. IRWIN: Gentlemen, this is a memorandum reporting the details further to the verbal report I gave to the Committee on July 29th, as a result of directions given to me by the Committee in December of 1963 to further enquire as to the practicability of reducing the various costs of borrowing to a rate percent per annum.

Just as a preface to this,I had prepared this on September 14th, 1964 and it was a coincidence that it appeared before you at the same time as Professor Ziegel's comments.

Memorandum in respect to mathematical and administrative aspects of calculating the cost of borrowing as a percentage rate. The subject matter herein is concerned with mathematical and administrative problems involved in the determination and disclosure of the cost of borrowing expressed as a rate percent of the principal sum. The Committee has received representations to the effect that (a) in certain cases it is difficult if not impossible to determine accurately the cost of borrowed funds in terms of a rate percent per annum, (b) that if such disclosure were required serious administrative difficulties would be created, (c) that disclosure would not be comprehended readily by the borrower. Certain other arguments in opposition to such disclosure have also been advanced.

(a) that in certain cases the charges made are not interest but represent service costs and other expenses; (b) that disclosure would result in a transfer of costs for money to the price of the article. This memorandum does not deal with considerations of public policy but is confined to an assessment of these representations as they may bear upon mathematical and administrative feasibility.

Definitions and assumptions. It is necessary to define certain meanings and comment on certain assumptions which commonly occur. Interest versus the cost of money. The cost of borrowing money, or credit, includes values in respect to (1) pure interest, (2) risk, (3) service costs and (4) direct outlays, for example, legal fees.

Pure interest is an economic concept of the value attached to the use of money per se. It is a rent paid by the borrower to compensate the lender because he must defer the satisfaction of wants which immediate use of the money would otherwise bring. Pure interest rarely exists. Perhaps the closest approach to pure interest is found in the case of a government Treasury Bill in regard to which service costs, direct costs, and risk are practically non-existent. It is argued that the cost of borrowing money should not be called interest because of the presence of the other factors in cost. However, the term interest is in common use -- e.g., commercial bank loans and by insurance companies in respect to mortgages even though factors other than pure interest

are present.

On the other hand, lenders on conditional sales contracts obdure use of the term interest on the grounds that their charges are for service. These different viewpoints appear to be matters of degree rather than of substance insofar as except where pure interest occurs every charge for the use of money includes in some measure at least three of the elements mentioned above.

The non-interest contention may perhaps be resolved by avoiding any reference to interest and referring only to the cost of borrowing or the cost of money. If this premise is accepted we may escape philosophical arguments and concentrate on the problems of expressing the cost of money as a percent per annum or per period related to the amount of the principal advanced or to the balance of the principal unpaid from time to time. In this memorandum, for purposes of illustration and calculation, all of the four elements of cost are deemed to be included.

Methods of calculation. There are several methods used to calculate cost of money as a rate percent. Those in more or less general use are: (1) constant ratio -- a short cut formula which gives an approximation of the rate but which becomes more inaccurate as the terms of the contract are longer the ratio of finance charges to principal becomes higher. (2) direct ratio -- a short cut formula giving an approximation of the rate more exact than the

constant ratio formula but still subject to margins of error which could lead to dispute.

(3) Add-on and yield formulae -- a percentage added on to the principal. These forms are used by those who expect a certain percentage yield return which is converted to a simple arithmetic add-on by use of tables. The tendency is to round out the add-on percent to even dollars and to apply the add-on dollars to ranges of loans within, say, ten dollar intervals. The actual rate charged may vary significantly between that applicable to the loan at the lower end of the range and that applicable at the higher end of the range.

(4) Many variations of the foregoing methods, which are subject to the same criticisms. Many lenders develop their own formulae. This is just to cover the infinite number of formulae which are developed for special purposes and they are short cut formulas. There is one which came to our attention from the mortgage lenders called the "in-gray" formula. And you will find this in almost every phase of lending that someone has developed a formula on a short cut basis to interpret to themselves the yield rate. This isn't necessarily conveyed to the borrower.

(5) Simple interest calculations on a daily or other periodic basis with or without compounding.

(6) The actuarial method. This is a general term describing methods used by actuaries to determine rate percent employing higher mathematical

formulae. For practical use standard tables derived from these actuarial formulae have been developed and are readily available. In addition, actuarial tables to suit special purposes may be obtained from several publishing houses and actuarial organizations. In fact, such special tables are in general use by lenders. Here is a book which contains standard actuarial tables put out by the Chemical Rubber Publishing Company, and these tables are used in the insurance field and in almost every field where the calculation of a percentage rate is required. The tables cover a number of, or represent specific calculations using a number of different actuarial formulae. For instance, a table on the present value of one, an amount of one at the end of a certain time, the amount of an annuity of one, the present value of an annuity of one, an annuity whose present value is one, and so on and so on.

Accuracy of method. It has been submitted that if you ask six different people to calculate the true rate of interest in regard to the same loan contract, you may get six widely different answers. The inference is made that this demonstrates the futility and inaccuracy of making the calculation at all. This criticism is a half truth. Because of the number of different methods it follows that if each of the six calculators use a different method, different results will ensue. Furthermore, some of the calculators may make different assumptions as to (a) the exclusion of some of the elements of the finance

charge. For example, legal fees might be excluded. (b) The compounding of interest. In regard to (a), that is the exclusion of elements, it is obvious that for purposes of comparison none of the factors may be left out of the calculation. In regard to (b) compounding should not be assumed unless it does, in fact, take place.

Certain tables are available which are based on compounding at periodic intervals. That is, daily, weekly, monthly, quarterly, half-yearly or yearly. These tables are, in turn, sometimes applied incorrectly in respect to contracts which in reality do not include a compounding feature. When this is so the rate derived from the tables will not reflect the true rate applicable to the contract.

Compounding occurs only if interest is charged but is not paid. That is, interest is carried forward. In most instalment payment contracts for example, interest is paid as it accrues and no compounding actually takes place. It is a question of fact in every case whether or not compounding occurs. Lack of precision in regard to compounding may be corrected by exact stipulation in the contract.

In presenting a problem for solution to the six different calculators, the following should apply. (a) The terms of reference must be exact and identical for each calculator and (b) each calculator must use the came method. If these conditions are met the six calculators will produce six identical answers to the same problem. Similarly these conditions

being applied to six different problems, the six results will be mathematically comparable.

It follows from the above that if all lenders were required to use the same method of calculating the cost of borrowing as a rate percent, a borrower would be able to make a valid comparison between the rates offered by lender A or lender B for an otherwise identical loan. Legislation, if enacted, covering disclosure of cost of money as a rate percent would need, therefore, to establish a common terminology and a common basis for calculation of universal application.

Selection of method. In respect to mathematical methods, loan arrangements may be classified into general types. (1) contracts requiring specified payments of principal and specified rates or amounts of interest -- that is, cost, -- each paid separately. For example, a commercial bank loan or a non-amortized mortgage. These are essentially simple or compound interest problems resolvable by arithmetic.

(2) contracts requiring blended payments of principal and interest;for example, conditional sales contracts and amortized mortgages. These are resolvable by use of actuarial methods.

(3) contracts which are a combination of (1) and (2). As will be explained, a revolving credit account is not readily reducible to simple, mathematical formulae. In respect to all other loan contracts, a rate percent may be determined by methods

(1) or (2) or a combination of both.

Review of the various methods available leads to the conclusion that use of actuarial methods only provides means of calculation having universal validity in cases where simple interest calculations are impractical.

An important point to observe is that while it may be a difficult mathematical exercise, to deduce the true rate percent from a stated case wherein the amount of finance charges is given but in which the rate is unknown to the calculator -- that is, the borrower -- it is a relatively simple exercise for the lender to select and state the rate to begin with and to derive therefrom the total finance charges applicable.

In other words, forward calculation from a stated rate to total charges is infinitely less difficult than the mathematical difficulty of deriving an unknown rate from the stated charges.

The actuarial method. We need not belabour the mathematics of simple interest calculations but the actuarial method requires some explanation. From here on Itried to make this in the simplest possible terms and language, so if you don't see any formulas it's because I didn't wish to put them in.

Instalment contracts of blended payments of principal and interest, for example an amortized mortgage, a conditional sales contract, are mathematically equivalent to annuities in one form or

another. The principal sum is, in effect, the present value of an annuity to be received. Actuarial tables express this as the present value of an annuity of one with interest payable in arrears. If the rate per period is unknown but all other factors in the problem are known, the rate may be determined from these tables. That is, these standard Rubber Chemical Company tables and those tables specifically dealing with the present value of an annuity of one.

Standard tables of this type, however, are produced on the basis of intervals in the rate of 1/8th of 1% per period in the lower ranges, intervals of 1/4th of 1% per period in the middle ranges and 1/2 of 1% per period in the upper ranges. In other words, the standard tables that are available and are in common use everywhere move at these intervals. In other words, you can read off the rates, but the rates move from 1/8th to 1/4th to 1/2 and so on and in between you are left absolutely uninformed as to what a marginal rate in between the given rates may be.

Where compounding does not occur -- for example, a monthly rate of 1%, may be expressed as a nominal annual rate of 12% chargeable monthly. This is from the table. The next higher rate in the table -- the presently available table -- is a rate of $1\frac{1}{4}$% per month. Then if you want the annual rate from that, that becomes 15%. And the difference is 3% per annum. Obviously the actual rate of a given problem might lie somewhere between 12% per annum and 15% per annum and use of either rate would be substantially

inaccurate. In other words, if you rely on the presently available tables you could be out by 3% per annum.

In the interest of greater accuracy it is necessary to create actuarial tables with very much narrower rate intervals. The writer has, therefore, evolved and caused to be produced actuarial tables for the present value of an annuity of one dollar, payable in arrears at rate intervals of 1/100 of 1% per period, for example, per month. These tables result in annual rates moving at intervals of 1/8 of 1% per annum. The margin of error for the annual rate cannot therefore exceed 1/8 of 1% per annum. The range covered in these tables is from 1/2 of 1% per period to .0257% per period, or slightly over 2½% per period and from 1 to 120 periods. I think I showed you these before. These are the tables we had in July.

These tables have been produced experimentally. They could be further refined to produce annual rates with margins of error of 1/16th, 1/32nd, 1/64th, etc., of 1% per annum. Disclosure within an accuracy of within 1/8 of 1% per annum might be considered sufficiently valid for purposes of comparison.

MR. WHITE: May I ask a question?

THE CHAIRMAN: Would you agree to answer a question now?

MR. IRWIN: Oh, sure.

MR. WHITE: Well, this relates to

something that was brought up before. Mr. Sedgwick, if I remember rightly, you said that you were in some doubt as to whether legislation could require the disclosure of interest within a certain tolerance. Have you looked into that?

MR. SEDGWICK: I haven't looked into it with any care, but I think that you could validly legislate saying that the interest shall be disclosed to 1/8th or 1/4th. I don't think that would be invalid.

MR. WHITE: What about mortgages?

MR. SEDGWICK: It is precise. It is always precise. You would have great trouble in enforcing your mortgages if it were not precise because in the case of arrears, as you well know, you must collect the precise rate. But I'm not talking about the rate to be collected; I'm talking about information to be given to the buyer. You are not going to collect the 17-1/8. I assume that there will be in the contract, if this should become legislation, saying the dollar amount of the charge under this contract is $50.00, the approximate annual rate percentage is so and so. Now that doesn't mean you are going to collect it, it only means that you are giving him information. You are going to collect the $50.00, but you are telling him the $50.00 represents an approximate annual rate of so and so. I don't think you could make an imposable document with an approximate rate if propose to collect the interest. That isn't the purpose of this.

MR. IRWIN: Use of the tables -- that is, these tables. I want to make one comment. These I produced experimentally. I don't visualize that this table would necessarily be the table which would be used in connection with this legislation. What it would -- if this legislation came to pass. But further practical working tables would develop from these and they would have to be accurate because they would have to be taken from these.

In the case of blended payment contracts, or aspects of contracts because some contracts have no features, the rate may be found using the tables as follows: (a) determine the principal advanced (b) the aggregate payable and (c) the number of payments. Now this information is already given in making up the contract for the borrower in closing the sale. So that information would be already at hand.

Now this whole scheme is mathematically correct but it is a short cut way of arriving at an accurate rate. You then multiply the principal by the number of payments -- that's number 1 in (a) times 3 in (a) and divide by the aggregate. That's 2 in (a). Then step (c) is a factor evolved from step (b) which factor may be found in the tables in a column of figures giving the monthly and the annual rate percent applicable to the number of payments in the contract. I will illustrate this later.

The writer does not suggest that a clerk making out a contract form should be required to

go through all of these three steps. Administrative burdens should be kept to a minimum. Business experience, however, indicates that the clerk now performs step (a) with tables now in use. The clerk could also be provided with actuarially based tables which includes steps (b) and (c). The clerk would perform essentially the same task but his new tables would not only provide the information presently given to the borrower as to the principal, aggregate, finance charges, payments per month all in dollars, but the rate percent per annum as well.

The specific applications. The classifications and sub-classifications of loan contracts may now be analyzed and methods suggested for determining rates applicable to each.

The Small Loans Act. The rates permissible by law are 2% per month of the first $300.00, 1% per month on the next $700.00 and ½ of 1% per month on the next $500.00. Determination of the overall effective rate for any given loan by deduction -- that is reducing the rate -- is a relatively difficult assignment. However, in consultation with one of the lenders under this Act it was found that their present tables were readily adaptable to the declaration of a yearly rate for all categories of loans offered by them merely by precalculating the rates and adding them to their present schedules. Very accurate and comprehensive tables are used by this lender which comply exactly with the Small Loans Act for any amount of principal outstanding for any number of periods and

the time you get to $982.56, which is that next closest before reacing $1,000.00, the effective monthly rate is 1.49 and the annual rate is 17.88. If we go right down to the bottom of the schedule the maximum amount that they are prepared to loan of $1,219.82, the effective overall rate -- that is including the 2% rate, the 1% rate and the ½% rate is 1.38% per month or 16.56% per annum.

Columns 6 and 7 include the insurance as part of the cost of borrowing and as you will see the rates are slightly higher after including the insurance premium, down to the $300.00 level, the rate per month is 2.08 and 24.96% per annum, and so on down to 1.45% at the lower end of the table or 15.40% per annum.

Now in actual fact, of course, in my working papers I have got eight places of decimals for each of these rates and these are to the nearest second place of decimals.

Conditional sales contracts. Several retailers were requested to furnish information as to their present methods of determining finance charges and examples of actual loan contracts have been compiled. In all cases there were three such retailers who each supplied 12 contracts and I asked them to pick out the most difficult ones that they could find. In all cases these contracts are found to be reducible to annuity problems and rates could be determined from the present value tables. Tables are presently in use based on the add-on principle.

In other words, everybody has a table which shows that if the amount being loaned is $100.00 for 12 months then add-on this amount and that the clerk does. The effective rates percent are not given. In the final analysis it has been found that the effective rates vary significantly in respect to dollar amounts of loans bearing the same add-on. In other words, this is a matter of administrative convenience that they don't list every loan by dollars, they list is as between $100.00 and $110.00, say, add-on $10.00. I guess it is fairly obvious that a man that is in fact borrowing $110.00 with an add-on of $10.00 is paying a lower rate than a man who is borrowing $100.00 and being charged $10.00. There can be a significant variation as high as 10 and 15% because of using ranges of loans with the same add-on.

Revised tables could be prepared showing effective rates within narrower ranges of loan balances based on actuarial tables. The procedures to be employed to determine an effective rate percent are demonstrated in respect to an actual loan contract as follows: This is an actual contract, given to me by a retailer. The amount borrowed was $256.77, the finance charges added were $45.00 and the aggregate to be repaid was $301.77. Payments required were 17 at $17.00 for $289.00 and one of $12.77 making up the total of $301.77. Now the average was not given, that is my own figure. There are 18 payments averaging $16.76.5 as the additional decimal. Now using the procedure described in table 10,

we multiply the 256.77, the amount borrowed by the number of payments, 18. And this gives us a figure of 461.86. Then we divide that figure by the 301.77 and this produces a factor of 15.315836. Now I want to reemphasize in doing it this way I am demonstrating mathematically how it can be done accurately under the actuarial method. As stated on page 10, further tables would carry out these preliminary calculations, to get the rate.

So we get a factor of 15,315836, so we look up on the table for 18 payments and we find a factor of 15.28611734 which is a rate, which is shown at the top of the column of 21.12% per annum. So what I am trying to demonstrate is that here is the information. Further tables would make this calculation to produce this factor. You look up the factor and there is the rate.

The same factor is also produced by dividing the principal of 256.77 by the average payment of 16.765. The rate would be the same -- 21.12% per annum.

The exact rate in the above problem is slightly higher than 21.12 which is read from the tables because the last payment of$12.77 is considerably below the level of the other payments. In fact the exact rate is 21.3% per annum. What we have here, in effect, is two annuities. One at a level payment of $12.77 and another at a level payment of $5.00. This inaccuracy may be eliminated if regulations were to require no payment may differ from the average of all

payments by more than, say, 10%. Now this is from a mathematical point of view absolutely essential. You would have to provide that the variation of any one payment should not exceed 10% of the average of all payments, otherwise you could get errors greater than 1/8 of 1% per annum, as I illustrated above. But if this rule applies then you would be within an accuracy of 1/8 of 1% of the true rate.

Mortgage loans. This is a fully amortized by maturity mortgage. All charges, including legal fees are included in the calculation. This is in line with the premise that mathematically speaking you have to include all the charges if you are going to make comparisons. Or you would have to, in all calculations, exclude some, if that is the way you wanted to go about it. But at least they must be consistent. Now for purposes of illustration I say that they are all included.

Note where there are no charges other than interest the stated rate is the effective rate. So to deal with an example -- the principal borrowed is $10,000.00, the legal fee is $100.00, other fees $35.00 and the net that the borrower gets is $9,865.00. The stated rate is 6% per annum, the term is 10 years, it's fully amortized in blended payments of $111.02 per month for 120 months and the aggregate of all those payments is $13,322.46. So the solution is to determine the actuarial factor. If 9,865 is the present value and $111.02 per month for 120 months, the factor is 88,857,4632. Again we just look at the

table for 120 payments and the factor of 88857 is 6.36% per annum. The exact rate is 6.30%, but 6.36 is more accurate than either of the nearest other table rates of 6.24 or 6.48. Again you are within the accuracy of 1/8 of 1% per annum.

In a mortgage loan in which there are blended payments but with a balloon payment at maturity. Part of the principal is amortized over a term and the balance being due at maturity. Note (a) where there are no charges of any kind the stated rate is the effective rate; (b) where there are other charges we have two problems, an effective rate to maturity on the amortized portion and the stated rate on the balloon payment.

Example -- a 6% 10 year mortgage of $10,000.00 with $5,000.00 remaining at maturity. Principal payable over 10 years is $5,000.00. The cost is $120.00, the net received is $4,880.00 plus the $5,000.00 balloon. The loan is payable of the $5,000.00 principal in blended payments of $55.51 per month plus interest on the balloon. The aggregate of the blended payments is $6,661.23 so that $4,880.00 received by the borrower is the present value of $55.51 for 120 months. Again we get a factor for 120 payments, we look up the table, and we find a rate which is 6.48% per annum, actually the rate is 6.54 -- that is, the table shows that, but for purposes of reporting herein, I calculated the exact rate in respect to the amortized portion of the loan. Once again this is within 1/8 of 1% of the true

rate. The stated rate of 6% applies on the balloon payment portion.

Now there is a mortgage loan that is fully amortized with bonus and other charges. A 6% mortgage payable over 10 years, the principal amount is $10,000.00, the bonus is $2,000.00, charges of various kinds $1,000.00, net deduction from the principal is $3,000.00, net cash received by the borrow is $7,000.00. Payable over 120 months at $111.02 per month the aggregate payable is $13,322.46. $7,000.00 of a present value of 120 payments at $111.02 per month. We get a factor of 63.05141843 and we look up the tables for that figure and we get 14.52%. Again the actual rate using actuarial methods independently of the table is 14.55% -- again within an accuracy of 1/8 of 1% per annum.

Mortgage loans that are partially amortized with bonus charges. An example is a 6% mortgage of $10,000.00 payable, with $5,000.00 amortized over 10 years and with a $5,000.00 balloon at maturity 10 years hence. Again the loan breaks down into two parts, the amortized portion of 5,000 and the balloon or the amount dueat maturity of 5,000 and in this case you deduct the bonus and the charges with a total of $1,800.00 from the amortized portion. The net received by the borrower is $3,200.00 in regard to the amortized portion, $5,000.00 in respect to the balloon or $8,200.00. This is payable as to the $5,000.00 amortized at $55.51 per month for 120 months plus interest on the balloon. The aggregate

payable again is $6,661.23 for the amortized portion and the rate on the amortized portion gives a factor of 57.64701 or a rate of 16.94% -- 16.92 from the tables -- and the actual rate is 16.94. Again within 1/8 of 1% per annum. The rate on the balloon is the stated rate of 6%.

You will observe that I am using the same rates and figures in each illustration so that we don't get off onto a whole lot of other calculations. But this doesn't invalidate my conclusions.

MR. WHITE: You can combine the interest rate on each of these forms into one figure I suppose?

MR. IRWIN: That would take another calculation. I didn't put that in here.

MR. WHITE: You might want to do that.

MR. IRWIN: I think what I am trying to illustrate is it is not all that hard to develop the formula and the tables to do whatever you wish with this thing. I could have made this incomprehensible by adding all kinds of possibilities.

Non-amortized mortgages. Where the principal is paid separately and interest is calculated and paid separately then the rate of interest charged is known to the lender. Otherwise the finance charge is purely arbitrary and the rate must be derived. In other words, I have found it so that the lender knows what he is charging in terms of a percentage rate. In any case that I have run into this is true. What

may arise in the odd case is that the lender may just pick a figure in absolute dollars as to what he thinks the traffic may bear and even he doesn't know the rate. But where a person is in the regular practice of lending money, he knows what rate percent he is using to calculate the finance charge total in dollars. Representative types are (a) a non-amortized mortgage with no bonus, and no charges, in the stated rate. There is no problem in this case as the stated rate will be applied to the unpaid balance from time to time and will, in fact, be the effective rate. This is just a straight loan with a stated rate of interest and the lender applies this stated rate to the balance from time to time and calculates out the dollar amount of the charges and adds it to your account. There is no special calculation to be made here whatever.

The second type under the non-amortized loan is a non-amortized mortgage with a bonus and charges. An example is a loan of $12,000.00 payable over 10 years, as to principal, at $100.00 per month plus interest at 6% charged and paid as accrued and subject to bonus and other charges. The principal borrowed is $12,000.00, the bonus is $2,000.00 and the charges $1,000.00, total deduction $3,000.00 and the net received $9,000.00. Now here you use a slightly different method involving the tables -- it would have taken several extra further explanations and I don't think it is terribly important to burden you with that. I can assure you that it isn't very

difficult to do. By factoring the account at .05% per month we determine the total interest charged on the $12,000.00 for 10 years is $3,630.00 and this is quite a simple calculation. The total cost of borrowing $9,000.00 therefore are $6,630.00, that is the borrower is paying $3,000.00 for charges and$3,630.00 for interest. The total payments amount to $15,630.00. By the use of algebra we determine that the 9,000 at the present value is the sum of all the payments with interest at .0113% per month, again this is taken from the tables, or a nominal annual rate of 13.56% per annum chargeable monthly.

The skipped payment contract. These problems are of two types. Payments defaulted by the borrower and deferred payments written into the contract. Defaulted payments defaulted by the borrower by design or accident pose no significant problem. Once the effective rate is known,and in most cases it is known to the lender, and if it isn't known it may be derived by the methods that I have described, that rate may then be applied to the principal included in the defaulted payment for the number of days defaulted and thus determine the additional charge in dollars.

Now deferred payments written into the contract present no problem either if the rate is known to the lender. And in the vast majority of cases, I would go so far as to say, 95% of the cases, the rate is known to the lender. This is how he operates. He knows what yield he wants and he

applies this to each loan. Additional interest charges in respect to deferred payments may be calculated as in the foregoing paragraph. In other words, if the lender knows the rate then all he has to do is make a simple interest calculation for the number of days of default and add that to the account. This is whether the default is initiated by the borrower or is written into the contract at the beginning. If the rate is not known then it must first be derived by the methods I have described.

If they are required to derive a rate from a stated case the mathematical problems are more difficult. This is where presumably the lender doesn't know what rate he is charging. For example, and this example is taken from the submission by the Automobile Dealers Association advanced by them as indicating how impossible it would be to find the rate.

This is an automobile sold to a teacher. The amount to be financed was $2,400.00 and finance charges were $460.00. The aggregate to be repaid was $2,860.00, to be payable at $100.00 per month from February, 1962 to September, 1964, both inclusive, but not for the months of July, August and September, 1962. This is a deferred payment written into the contract. There are 28 payments of $100.00 and one payment of $60.00. The average payment is $98.62. Here again you would have to provide, if you want the rate produced for disclosure, to be within

1/8 of 1% of accuracy using these actuarial tables. You would have to provide that no payments could vary from the average payment by more than 10%. In this case it does and the rate is marginally different than what I produce here. The average payment is $98.62 per month. The procedure is you factor the account in regard to the skipped payments. Now remember this -- you are going through a whole lot of motions here that aren't necessary because if the lender knew what rate he was charging that would be it. But because certain people have advanced it as to how you figure the rate on this complicated situation, you have to go through all these motions. And they are totally unnecessary in practice. This is merely an exercise to show that it can be done.

You factor the account in regard to the skipped payments, that is the July, August and September payments, are each deferred 24 months. So therefore the lender is out of pocket $100.00 for 24 months three times. The factor of this is the equivalent of $7,200.00 for one month. The interest charged on $7,200.00 is X -- we don't know it. Now the $2,400.00 -- the amount financed -- has a present value of something, and it's the present value of the $98.62 payment, 29 of them, less the amount of interest that is paid on the factored amount of $7,200.00. These are the skipped payments. Now we may solve this by algebra or by inspection. Using inspection, which is a common method used by actuaries, again using tables. They say, well, here is a complicated problem. We could

work it out by a long, complicated formula, but let's look at our tables and assume the closest rate we can identify and see what that shows us. And nine times out of ten that is all they have to do. So assume a rate of 1% per annum -- that is roughly what the rate has to be -- the interest on $7,200.00 at 1% per annum for 1 month is $72.00. So we reduce everything by the $72.00. This is what was added on by the lender because of the skipped payment and we want to find the rate he used if he didn't have the skipped payment. So we revise the problem and show the principal borrowed was $2,400.00, the charges were $388.00 -- that is we are excluding the added charges because of the skipped payment, the aggregate is 2,788. Again we get a factor of 24.96413199, which we find in the tables for 29 payments of 1.03% per month or 12.36% per annum. Now in actual fact the rate used was probably 12% per annum with the charges rounded off to the nearest ten dollars. This very often happens. The man knew when he loaned the money that he was going to charge 12% per annum and he worked it out. I haven't checked this one because I don't know who was the lender, but I have checked others whom I do know, and in fact that is what they do. They say I am loaning 2,400 for 29 months and I am giving three skipped payments and I want to get 12%, so we look it up in the table and it comes out to some figure like maybe $451.67, so he says let's call it 460. So this means that he gets a very slight

increase in the rate. For all practical purposes he thought he was using 12% per annum and that's all he need state.

The next one is a truck sold to a farmer. This is the case of pity the poor farmer or pity the poor salesman dealing with the farmer. This again is taken from the Automobile Dealers Association exactly as they stated it. The principal to be repaid was $1,200.00, the finance charges were $138.00 and the aggregate of the payments was $1,338.00. Payments were to be made on the 13th of each month on September, October and November of 1962 of $200.00 each, then nothing paid until April and May of 1963 when he made two payments of $100.00 each, nothing further paid until September and October, 1963 when he made payments of $150.00 each and then in November, 1963 he paid up the whole balance of $238.00 and all other months are skipped. Now this is a contract written intentionally with deferred payments.

Again I repeat that from my experience with lenders, the lender knew what the rate was, to develop the charges of $138.00 and taking recognition of the skipped payments and I maintain all he needed to have done was tell the borrower what the rate was because the lender knew what it was in the first place. But the problem has been put by the Automobile Dealers in the sense that there is a tough problem, how could you develop a rate? Well, it's not that hard.

This again is a problem in factoring. The principal outstanding from month to month is the

equivalent of $8,400.00 outstanding for one month. So the $138.00 charges is the interest charge for one month on $8,400.00 which actually, using simple arithmetic, is 1.6428% per month or 19.7136% per annum.

Now I say note the foregoing is also a simplified version of more complex procedures used. I haven't put all my working papers here, but I have proven out that using that rate of 1.6428% per month and reconstructing the account, that this is, in fact, the true rate and produces $138.00 in total finance charges.

I repeat, however, that the lender undoubtedly knew the rate at the beginning. It's just that it is a little difficult to find out what rate he was charging in the sense of making it into a riddle. The common criticism of rate disclosure is that the salesman or clerk would find it extremely difficult to cope with the problem of disclosure and additional charges on interrupted contracts.

The foregoing illustrations are of this type so that a rate is determinable. This is the important point. The salesman talking to the farmer on the fender of his truck would certainly not go through this factoring process that I have done because he knows what the rate is. The office of the lender would and does predetermine the rate of charge and furnishes the salesman or the clerk with tables, the use of which, plus elementary arithmetic, provides the extra dollar charges for the skipped payments. In

other words, I know this for a fact that a little bit of simple arithmetic plus the tables which the salesman can be provided with, if he isn't, he should be because in most offices I have had any experience with they are available, would tell him that using a rate per month of this and a number of days lapsed, there is the amount of interest. I think I have pointed out to you the case of the small loans company. This is what the clerk has right beside her. They don't have to do any calculation to determine what was the principal of the skipped payment or the total payment, because he is entitled to interest on interest, and he looks up the table for 29 days elapsed for $100.00 and there is the amount that he adds to the account. I am speaking from my own knowledge of lenders that this is, in fact, what they do.

The problem of the salesman or the clerk is very much overemphasized. In practice additional charges on defaulted payments are ignored in most cases. This also is a business practice. The lender relies on his title rights and collection procedures and accepts a very slight loss of interest rather than make marginal calculations. In cases where the deferred payments are written into the contract the additional charges are precalculated by tables so the salesman or clerk is not normally required to make individual calculations on the spot.

Cycle credit accounts. Budget accounts. A budget account is one wherein a purchaser undertakes at the beginning to pay off a specific balance over a

stated number of months including finance charges. In other words, at the beginning of the budget account the purchase has been made, the amount borrowed can be determined from a table, the clerk knows what is required by way of charges for the number of months agreed to by the borrower, and it is quite easily written and the assumption is made at that time that that arrangement will be carried out as specified. However, the rate may be determined in the same manner applied to a conditional sales contract. If we don't know the rate, it can be determined, as under the conditional sales contract, because that arrangement is intended at that time, at the beginning, to be carried out as stated. So it is no different than a conditional sales contract at the moment.

However -- and this is the key point -- the buyer retains the initiative with the concurrence of the lender, to alter the contract by buying additional items or paying more or less than agreed. This is peculiar to budget and cycle accounts and quite distinct from the conditional sales contract.

Mathematically the rate can be determined in the same way but because the arrangement with the lender is that the buyer retains the initiative to change the contract, in effect, at any time, it means that the effective rate can change from day to day. In other words the rate which was determined at the beginning of the contract does not necessarily hold to the termination of the contract. Whenever the borrower thus alters the terms of the contract, a

new formula develops. Going back to the formula on conditional sales contracts, every time the guy makes a payment which is more or less than the amount specified, then the rate differs and a new calculation would be required or if he added to his account by making a new purchase, then an entirely new set of mathematical factors are involved and a new effective rate of interest applies.

Insofar as this initiative is exercised frequently perhaps monthly, even daily, it might be considered an onerous task to impose upon the lender to recalculate the rate each time the terms of the contract change. Some modification of rate disclosure may have to be considered.

One suggestion would be a percentage charge based on the current month's balance. That is as opposed to the previous month's balance, or the mid-month balance or the average balance. Now this doesn't result in an accurate rate prevailing throughout the entire month. It just means that the margin or error is reduced by using a more current balance.

MR. WHICHER: It's just as accurate as rates, for example, banks pay on savings accounts.

MR. IRWIN: Yes, in the same sense that is true. In other words, in the case of the bank that pays its interest on a minimum balance in a three month period, they just are not giving you any interest on some part of the balance.

Now, the revolving credit account. These are arrangements whereby the borrower or buyer is

permitted to carry balances up to a stated maximum and is required to make a stated monthly payment. Now here again, at the beginning of the arrangement the borrower confers with the credit department and somebody sits down with him and says: "Well, now" -- they get all the credit information and say: "We are prepared to permit you to run a revolving credit balance up to a certain level"-- \$200.00, \$300.00, \$600.00 or \$1,000.00 -- depending on their credit evaluation. And on that basis say: "We are going to allow you to run a balance up to \$500.00 and you will be required to pay \$25.00 a month" -- for example.

But the buyer retains the initiative too, and again can charge any amount any time and pay any amount any time. The lender makes a monthly charge based on the previous monthly balance. A period of grace is allowed in respect to payments received within three or four days after the previous billing date, otherwise no recognition is given in respect to the varying amounts of credit actually extended from one billing date to the next.

Action by the lender to correct or compensate for variations in the original terms are post facto. That is if you, say, ran over your \$500.00 limit they probably would let you go for a month and then you would be called in to have a talk with them as to carrying out the arrangements as originally provided. But I think it is a very important point that the lender at all times has the initiative. The borrow can only correct the situation after the event.

This distinguishes it from the written conditional sales contract or any other form of lending that I have run into.

It has been observed that finance charges expressed as a rate percent in these cases can be very high. And I deliberately avoid suggesting what the rate is because it would be totally unrealistic and quite unfair to make a ridiculous calculation, because I maintain this is not the fault of the lender. It is the nature of the contract that the borrower sets the rate -- unwittingly, it's true -- but the borrower, in effect, sets his own effective rate.

Now this is again an actual account. The previous balance on April 15th was $431.75. The charge on the next billing date, which was May 15th, the charge, which is taken from the table -- if you have a balance between $400.00 and $435.00, the charge is $4.95. So the charge of $4.95 would be made on May 15th. Now the rest is hypothetical to illustrate a point. If a payment had been made on April 20th, five days after the previous billing date, beyond the three or four days of grace, as I mentioned at the top of the page, whatever you pay after April 19th will not be recognized so as in any way to effect the charge being made on May 15th. Now the monthly payment required is $22.00, but the borrower in this case ignored this arrangement and in this case a charge of $4.95 would still be made even though the payment of $331.75 reduced the debit balance to only

$100.00, for 25 days of the billing month -- that is, from April 20th to May 15th. In other words, in this case the amount of credit actually extended was only $100.00 for 25 days and yet the charge was made the same. So you can imagine that the rate percent charged on $100.00 for 25 days is extremely high.

It may also hold true -- this is another case, illustrative case -- based on a real case -- if there had been no balance on March 15th, and a purchase had been made on March 16 for $431.75 and then the next billing date of April 15th rolls around and there is no charge made at all because there was no balance on March 15th. Then the customer pays up the whole account of $431.75 on April 14th. Then the next date rolls around, May 15th, and no charge is made because there is no balance on April 15th. Now in this case $431.75 was credit extended to the buyer for 29 days at no charge at all. In other words, the buyer sets his own rate. In such circumstances it is obviously unreasonable to expect the lender to determine the effective rate from day to day.

Now the only qualification I have made about that is that if they go on to electronic computers, which they may do in due course, it would be administratively feasible. But at the present time I would consider it a quite unreasonable burden to place upon those lenders using the cycle or budget credit to make the calculations daily.

There is no practicable method of resolving this problem by tables or mathematical formula. At any given moment in the account these tables could be used, but what I am saying is there isn't any short cut way of doing it. It would mean going over every account every day with these tables and determining the rate and I would consider that as being a rather ridiculous proposition.

Alternative solutions may be suggested for compliance, at least partially, with disclosure requirements in terms of a rate percent. These are requiring the statement of a monthly rate percent and/or annual rate percent along with or in substitution for dollar charges now given, recognizing at any given time during the month the rate may be somewhat different. Require one monthly or annual rate in place of a scale of charges. The schedules presented to us indicated that the effective rate on the previous month's balance, ignoring all these other complications, could vary from 24% down to 12% per annum. You might consider extending the period of grace for recognition of payments between billing dates. In other words, the practice now is three or four days, usually three days. Perhaps if they extended the grace period to 15 days then you would cut down on the possibility of incurring a rather high effective rate. It would substantially reduce the variation of the actual rate from the stated rate.

It has been submitted to the Committee by some lenders that the public wishes the finance

charges to be stated in dollars. Indeed, the public would not comprehend disclosure in terms of a rate percent. These opinions appear to me to be subject to more conclusive verification perhaps by sampling consumer reaction on a substantial scale. The only point I am making here is that everybody states this but nobody seems to have proven it one way or another and I would be quite open to having that done and abide by the results of it.

Certain observations may also be made in regard to (a) disclosure of a rate percent need not be a substitute for a cost stated in dollars but in addition thereto.If the public does in fact prefer the cost in dollar it would in no way be hampered by being given the rate in percent. I have since read the Porter Commission on Banking and they say much the same thing. (b) The cost of borrowing is still being taught in school in terms of a rate percent. I have checked this with the curriculum and this is still true. Many types of loans are still being quoted as a rate percent, e.g., conventional mortgage loans and commercial bank loans. The average householder is likely to have been exposed to a rate percent in some instances. He also may be expected to have borrowed on a conditional sales contract in which only dollars costs have been stated. If the borrower has understood a rate percent as quoted by lenders of mortgages he might reasonably also be expected to comprehend the meaning of rate percent as quoted by lenders on conditional sales

contracts. It would seem that a common terms of expression in regard to both types of contracts would tend to reduce rather than to increase confusion. If expressed in the same terms the comparability of various sorts of lending would become possible.

Administrative aspects. Imposition of requirements for the disclosure of money costs as a rate percent might impose administrative problems and the impact of such burdens should no doubt be minimized. I must say I am quite concerned about this. Whatever is done should not impose administrative burdens.

It has been found that the determination of finance charges is now performed by clerks furnished with readily interpreted tables. It is submitted that the determination of a rate percent may also be revealed by the use of tables. This being so, administrative problems would not be significantly enlarged. It has also been found that in almost all cases these tables are based on a rate known by the lender. It would appear that the disclosure of this rate would not present a major difficulty.

Transfer of money costs. Disclosure of money cost as a rate percent may result in a transfer of some part of this cost to the price of the article. Lenders on conditional sales contracts might consider this to be competitively beneficial to reduce the finance rate and recover any loss resulting by an increase in prices. This type of adjustment would only be available to retailers who are also

lenders and would not be available to lenders of money only. If disclosure of rates were generally deemed to be advisable, this method of apparent escape in limited sectors should not invalidate the desirability of such disclosure in respect to all other lending forms.

In the retail field one may assume that a double competition of finance rates and prices would ensue. Such competition would eventually result in equilibrium. The buyer would be required to make comparisons both as to rate and price as between vendors, but at least such comparisons should be valid. This would appear to be more comprehensible than at present when apparently low prices may be offset by finance charges which are not readily measurable for competitive buying.

In conclusion, it is my observation that it is mathematically possible to determine the rate percent on all loan situations by the use of either actuarial methods or arithmetic methods. Practically, it would be an intolerable administrative burden to use the above methods from first principals, to determine rates on individual contracts, but rates may be readily determined for an individual contract by development of tables for universal application to all contracts of a specific lending classification, with the exception of cycle credit accounts subject to special circumstances. What I mean is that all tables used for practical purposes could be based on present values of an annuity of one, but for ready

reference each lending institution would no doubt develop their own tables for their own particular purposes. All the regulations would have to require is that they were evolved actuarially on the approved basis. And these could be checked out by the Superintendent of Insurance to see that they were, in fact, actuarially determined. But I am not saying that there could be one simple table applicable to all lending situations. Each lending type would no doubt want to develop its own particular table.

Disclosure requirements should be of universal application. The basic method of calculating rates should be determined for each classification of loan contract.

The use of tables would not appear to add a significant administrative burden insofar as tables are presently used extensively to determine finance charges. However, practical considerations suggest that the tables should permit a measure of tolerance when applied to a particular contract. The degree of accuracy of 1/8 of 1% per annum might be suggested, but this could be further refined.

A common language of expression and common criteria of measurement should be sought so that rates would be comparable. It would appear necessary that all elements of the cost of borrowing in all contracts must be included in calculations. In the case of blended payment contracts all payments should be nearly equal, say within a variation of 10% from the average.

Cycle credit accounts may have to be considered separately. If the buyer retains the initiative the lender may have to be permitted some tolerance in regard to disclosure of the effective rate applicable from day to day. Compliance with rate disclosure might be confined to declaration and imposition of a monthly and/or annual rate percent on the current balance or average balance.

Disclosure of a rate percent may be in addition to and not in substitution for disclosure in dollars, thereby providing for a common language and measurement without disturbing possible borrower preference.

THE CHAIRMAN: Any questions?

MR. ROWE: (Inaudible)

MR. IRWIN: I suppose it is quite possible. I suppose the comment on that is that you can't make any comment on it.

MR. ROWE: The salesmen have to do another job of selling. He sells the product first of all then he has to sell the paying of it. On the other hand, most people who finance cars now appreciate the fact that they are paying approximately 18%. Most farmers have trucks that they finance and they know that they have to pay about 20% and I don't think it would scare them for a tractor any more than for a truck -- a half ton truck --

MR. WHICHER: Mr.Irwin said he can make his own rate by this method of skipped payments.

THE CHAIRMAN: Mr. Bukator?

MR. BUKATOR: If the finance company tells me I can borrow a thousand dollars for my automobile and pay it in 12 months or 24 months or 30 months. I was wondering why they couldn't -- and this is my argument -- why they couldn't put this in a percentage of what I was paying for the use of that money. They simply send me to another source of revenue.

MR. IRWIN: Can't hear you, George.

MR. BUKATOR: I say they would simply send me to another source of revenue. You might have noticed on the subway, there is a prominent company there advertising automobiles for sale and they say you can borrow on your new car up to $3,000.00 and you pay a monthly payment of X dollars for 12 months or 24 or 30. I then felt that many people who ride that subway and read this particular thing, and if they inserted that other figure that I have been hollering about all these years, and I believe it should be there -- that the man should know exactly what percent, what amount it costs him -- is it 19% or 24% or 7%. I think it would send me to a bank or some other institution to shop around for money rather than the automobile. And I think this is good.

A few months ago, Mr. Irwin, the problem was could we come up with tables that would simplify the matter. I think that the sales people for automobiles alone -- which is a complicated one -- could carry a pad of tables around in their -- if I

wanted to sell that tractor to that farmer, you can depend on it that I would have every answer for him -- and if the tables are worked out -- the calculations certainly an actuary has to work out -- a man who knows, it's his business. But if you can simplify the matter and put it down -- $110.00 a month, 19% would be paid -- it would give that man a chance to look the thing over and say: "Well now look, I don't want to pay 19" -- or he may want to because he can't get it from another source. But it gives him a chance to compare. If we can come up with simplified tables then I think it is the answer to the problem. And I might say, Mr. Chairman, as far as I am concerned we can recommend to the Legislature in this session that we reveal the percentage rate. I don't think we have to go any further.

MR. WHICHER: Mr. Chairman, to back up what George has said, may I remind you there is a lot of life insurance sold in the back concessions. And when a fellow may be leaning over the tractor and the life insurance salesman is there, and when he wants to know what that premium is he's got the answer right there. It would be just as simple to have the answer as far as tractors are concerned, what percent it would be.

Mr. Chairman, I just wanted to ask one question. I think Mr. Irwin did an excellent job on this brief. I can't help but feel though that -- I know this is in your conversation too and in your brief -- where you are very worried about the cycle

credit accounts. Now actually I can't see why we should be so worried. We had the example this morning where Mr. Rowe said about stock brokers. Now this is a source where there is a great deal of credit, where many accounts I would imagine would be thousands and thousands of dollars. These are computed on a daily basis. Now if Roth Knowlton Company and A.G. Ames can do it, the T. Eaton Company can do it and if they haven't got calculating machines they can buy them, because nobody is going to tell me that they haven't got them already. They are there. And on the other hand, if they can't for some reason, they can then do exactly, in my opinion, as the banks do. They can take some standard -- whether it be the balance on the 15th of the month or the end of the month, the minimum balance or the maximum balance -- but all would have it the same in any event. The public know what it is and they might try to keep the amount owing down at that particular period. But to me a stockbroker's accounts is just as loose, as far as the buyer is concerned -- as long as his credit is good you are not going to stop him from buying stocks, he can buy four or five stocks --

MR. ROWE: You don't worry about his credit.

MR. WHICHER: I beg pardon. You don't worry about his credit?

MR. ROWE: You keep his stocks. (Laughs)

MR. WHICHER: But they also have to get paid the interest and this is computed on a daily

basis.

MR. ROWE: I omitted one thing, Mr. Chairman. I do want to compliment you, Mr. Irwin, on the work that you have done.

THE CHAIRMAN: Mr. Oliver?

MR. OLIVER: Well I was wondering, Mr. Chairman, we have, for instance, a number of lending institutions apparently that we are not competent in the Province to deal with. The banks -- now what others would there be? Trust companies, I suppose?

MR. SEDGWICK: It would certainly be the banks. That is the largest segment.

MR. REILLY: The Small Loans Act?

MR. SEDGWICK: Well, of course you have the Small Loans Act which the Dominion deals with. And that governs all these companies such as Household Finance who lend under the Small Loans Act. They comply with the provisions of that Act.

MR. REILLY: Under the circumstances, Mr. Sedgwick, the case that Mr. Bukator mentioned, of course, it wouldn't be necessary to show the interest percentage?

MR. SEDGWICK: No, that is true.

MR. OLIVER: That is just the point that I was going to make. When we talk about banks and trust companies, isn't it pretty well known what the banks charge?

MR. SEDGWICK: Well, it isn't known really, because they say on little loans of this kind

that they only charge 6%. They don't. They charge -- what would it be, Mr. Irwin --11½?

MR. IRWIN: Around 11.

MR. SEDGWICK: Yes. Once again, we, I do not think, have any legislative competence to regulate rates, only disclosure. That is a federal matter.

MR. OLIVER: What I am trying to get at is, say, for instance, we establish that the effective rate is -- not for the banks but for the other lending institutions -- say --

MR. SEDGWICK: That I don't think we can do. I don't think we can --

MR. OLIVER: I don't mean for the banks. I mean for other institutions.

MR. SEDGWICK: No, no. I don't think we can say that to anybody what interest rate they can charge. But what interest rate are you charging? That we can say, yes. But I don't think we can compel them to charge 8%.

MR. OLIVER: But once it has been revealed what the other institutions are charging, then it seems to me the comparison with what the banks are charging becomes rather obvious. I don't see that our failure or our inability to deal with the banks is going to jeopardize this legislation as materially as you think it will.

MR. SEDGWICK: Except that -- I'm going to be the Devil's advocate for a minute -- the argument on the other side is that if we cannot compel

the banks to make disclosure and they continue to talk about 6% when they are really charging 11.5, it would be most unfair to say to the Household Finance, for instance, you are charging 12 and you must say so. Because the man on the street thinks 12% Household Finance, 6% the bank, and that isn't so. You see my point? I'm only putting forward the argument that the finance companies will give you.

MR. WHICHER: Mr. Sedgwick, you mentioned to Mr. Reilly a minute ago that we could not control Household Finance who are operating under the Small Loans Act.

MR. SEDGWICK: You can't control that aspect of it because they come under a federal statute.

MR. WHICHER: But the point is that we have seen a copy of their promissory note and it is revealed there.

MR. SEDGWICK: I know that. And the percentages given there are taken straight out of the Small Loans Act.

MR. BUKATOR: They are required to do that under the Act?

MR. SEDGWICK: Yes. So much up to 300, so much up to 700, so much above.

MR. BUKATOR: I was wondering if they suffer by the fact that they reveal that percentage?

MR. SEDGWICK: I don't know. They don't reveal it as an annual percentage. They reveal it as a monthly percentage.

MR. WHICHER: They put it in an annual

rate.

MR. SEDGWICK: Do they? I don't think they have to.

MR. WHICHER: But they do. 24% per annum.

MR. SEDGWICK: Those rates are in compliance with the Small Loans Act.

MR. BUKATOR: This is all I ask for for the rest of the companies to do who do business in money. I can't see why they can't also do the same thing, because this is a competitive field. Why would I pay somebody 24 when I can get it for 12. This is why I want the public to know. From there on in if they want to pay a friend of theirs who is in the appliance business 36%, all right. But they should know what they are paying.

THE CHAIRMAN: The question was asked how much has it hurt Household Finance?

MR. SEDGWICK: I don't think it has hurt them at all. I don't think it poses any great problem with Household Finance and the lending institutions, but it will be met by the argument on the part of the sellers of merchandise that they aren't lenders of money, they are sellers of merchandise and that the lending of money or the extending of credit, as you may call it, is secondary and they would prefer not to do it. Then we had the example of the man -- I have forgotten his name -- who negotiated some of his paper and carried some of his paper and I assume there may be a considerable number of fairly well-to-do

salesmen of appliances and motor cars and so on who to a limited or to a great extent carry their own paper. I suppose they will contend that it means this witness can contend that he is in a position of saying how much he thinks he should get because he sees what the finance companies are charging and probably charges a little less rather than give credit. But he isn't in a position to say what that is expressed in percentage terms because he doesn't himself know. A great deal of that goes on. A great many appliance dealers will sell you a refrigerator and carry the paper themselves. They just add an add-on which I suppose they take from the finance company as being an approximation.

I can see the distinction he made between people who are lending money, like Household Finance, and they of course have experts whose business it is to have tables and those tables tell them the percentages. But people who are selling goods are probably not so well equipped and a salesman is less well equipped to come up with a percentage.

THE CHAIRMAN: On the other hand they make the argument that large sellers of goods -- their argument sounds a little hollow when they do it in some jurisdictions.

MR. SEDGWICK: Well no, they don't -- Mr. Irwin stated it quite accurately -- they don't determine an accurate daily rate. All that they tell you is that on the balance that you owed at a certain fixed date you will be charged arbitrarily 1½% the next

month. Isn't that right? Now it may be that in between you have paid the balance off, but you are still charged it. Or it may be that you owe something on that date and you have gone $400.00 over it since and you are charged nothing. But they don't attempt, as do the brokerage houses, to find an accurate day-by-day interest.

MR. WHICHER: I thought the Professor made that point very well this morning. Some people can take advantage of that 29 days over a period of time?

MR. SEDGWICK: That's right. They can be getting their credit free. And those of us who pay cash are presumably paying for it for them.

It is a very valid argument -- and Mr. Irwin said it, and I think probably accurately -- that up to 95% of the people who deal in money it would present no difficulty, but there would be a 5%, and the 5% is a little like the rotten apple in the barrel, they falsify all your conclusions, because you can't legislate the 95% and leave the 5% out. It may be possible, but it isn't simple.

MR. BUKATOR: I know I'm way out, Mr. Chairman, but the point that was made here this morning, and I may not get another chance to pick it up, was the fact that you may get the merchant who will hide the cost in the price of the item. Now some of the better -- I was thinking of the buyer that Westinghouse is selling -- and lo and behold I find that all of them have exactly the same price.

I was talking to the merchant who sold me my appliance at $129.95. That is pretty well fixed for the company. They wouldn't have any truck with dealers who handle their products for them, they would take that agency away from them, --

MR. SEDGWICK: That poses another problem, you see. They aren't allowed to fix the resale price by federal legislation. So I believe what they do is send out a recommended retail price and if you don't follow your recommendation, I think you are right, they don't give you a little --

MR. BUKATOR: They run out of the product or something.

MR. SEDGWICK: That's right, you are a little slow in getting your orders.

MR. BUKATOR: That can be controlled too eventually.

MR. SEDGWICK: Some people are trying to control it. It is very difficult to control because, as you know, there is a great deal of outside price making. A lot of people say it preserves the integrity of the product. That is the argument.

THE CHAIRMAN: Mr. White?

MR. WHITE: I have no questions.

THE CHAIRMAN: Mr. Letherby?

MR. LETHERBY: I haven't anything, Mr. Chairman, any more than to say, like others, I would like to thank Mr. Irwin for the very fine memorandum he has prepared. It has taken a lot of work and time. We have had so much controversy here

over our meetings as to whether we would like the amount of dollars disclosed in the borrowing of money or whether it would be feasible to give a percentage. I would just note here, Mr. Irwin, from your memorandum on page 4, at the bottom of the first paragraph. You say there "Legistation, if enacted, covering disclosure of the cost of money as a rate percent, you would need to establish a common terminology and a common basis for calculating of universal application". Now to me that sums it all up in a nutshell. If it were possible to reveal the cost of money in dollars and cents and then dash, as you say, George, this represents 5%, 8%, 15%, or 20%. But then I go back to what you said, Mr. Sedgwick, the man in the hardware store -- remember the appliance dealer? I recall very vividly his discussion and he was a loner to an extent, wasn't he? He was giving a certain --

MR. IRWIN: He knew nothing about actuarial methods. He just used --

MR. LETHERBY: No. He was just selling hardware that amounted to several hundred dollars. He knows his client, he makes his own arrangement, he carries his own paper. Now it would be difficult, I think, for a man like that to --

MR. IRWIN: This actually is no problem. Let's say I know this kind of man and operator and what he does now, in fact -- and I say this with all consideration -- he doesn't know what rate is being charged, but what he does do is he writes to a

publishing house and says: "Give me a table. I want to charge this kind of money -- 1% per monthly, roughly. Give me a table." And he gets the table and uses it. Now it is true he hasn't the vaguest notion whether this is an actuary account or not. But what I think I am trying to say is that if legislation required that such tables be based on the actuarial formula he still wouldn't know but he would then write to the publishing house and say: "In accordance with the legislation you must produce a table based on the present value of an annuity of one," without ever knowing what it meant. And he would get back a table based on that business and he would go on from there without ever understanding what he was doing.

MR. LETHERBY: I can see that wouldn't present any great problem. Just think of all those merchants in little hamlets, they have got their own tables for the 3% sales tax. To get the right answer and so forth they just go behind a door or wherever the table is and say it's so much money.

MR. IRWIN: I would like to make this comment on the sales tax because it is one that is a very good illustration in answer to this problem of the burden placed upon the small operator. The small operator, number one, is terribly ingenious and secondly he has associations who held him out. Now when the sales tax came into account I got phone calls all the time. The phone was ringing perpetually. "What am I going to do about this?" So we say hold on

for a week or two and we will work something out, or somebody will work something out. And invariably this is what happens. A person in the publishing business get a hold of this legislation and works out a simple, ready reckoner and distributes it. Then everybody is happy, they have solved the sales tax problem and the administration of it and it is satisfactory to the government and the consumer has got used to it and everybody goes on about their business.

I hope you realize that my study of the thing is stridly from the mathematical and administrative point of view, is it possible, is it feasible. I don't give a hoot what you do, but I do think it important that you understand whether it can be done. And I am quite confident that if such legislation came to pass this is exactly what would happen. If the legislation said no more than everybody must use a table using the actuarial formula of a present value of an annuity of one, well that would be the end of it as far as the Legislature was concerned, and within a week all the merchants in town would have these tables and they would be using them without ever understanding them, but they would be in business again.

MR. SEDGWICK: Well, Mr. Irwin, it does lead to another problem and that is the problem of enforcement. In some cases where the Legislature has prescribed conformity with certain tables, if you don't do it the contract is invalidated. Would

that mean that if a careless merchant put in 15% where it was 18% he would not be paid at all? Or would he merely lose the interest charges? Or would he be subject to prosecution and fine only? I don't know, but it is a problem of enforcement. You tell him to do it. What is the stick that you beat him with when he isn't a good boy. Does he lose his contract? Then the little fellow who is not familiar with it and relies on the table or puts his eye on the wrong line of the table and puts in 17 where he should put in 20 and then loses the money. It would be very tough indeed. I don't know what the method of enforcement is, but it is something that when you think of recommending so radical a change -- and remember we were told that no State in the Union and no Province of Canada and certainly not the United Kingdom has legislation of this kind -- so that we would be almost complete pioneers, you must look at the end of the road as well as the beginning.

MR. IRWIN: Could I comment on that, Mr. Chairman? I would like to make this comment, Mr. Sedgwick. I agree with you that there are many, many problems and I make no attempt to suggest that it is my province to suggest how the enforcement would take place.

MR. SEDGWICK: I'm not saying that to discredit you because I am a great admirer of your report.

MR. IRWIN: But in answer to this

problem, this is a puzzle to me. Why, in innumerable jurisdictions there has been a failure to grapple with this particular problem. I make this statement with some consideration and after some thought. I believe that the reason it has fallen down is that no such inquiring body has really grappled with the mathematical problem. You see --

MR. SEDGWICK: Oh, I think the Douglas Committee in the States did.

MR. IRWIN: Did they come up with a recommendation?

MR. SEDGWICK: Oh I think it has been grappled with a number of times and solved, if you can say that tables are the solution. But never solved pragmatically.

MR. IRWIN: This may be so. I have always felt in this that if the mathematical and administrative means of coping with the problem could be resolved, at least the pathway to the solution could be resolved, then you could get on to the real problems, which are the ones you are talking about. There may be a good many difficulties.

THE CHAIRMAN: Isn't it true that a great many people who have appeared before the Committee have said: "We don't object to it if you can show us how to do it".

MR. BUKATOR: I thought the Professor made a point this morning when he said meet the merchants themselves. (rest inaudible)

THE CHAIRMAN: What Mr. Sedgwick brings

up is another matter.

MR. SEDGWICK: You can't ignore it.

MR. IRWIN: There is one interesting thought though and this is strictly from observation of business over a number of years, Mr. Sedgwick. I have found that when a people are required -- say a man in business -- is required to conform to certain legislative requirements, he hates them but if he has to put his pen and his signature to them he will enforce himself, discipline himself. Now there is going to be the odd person who is going to beat it anyway, but so many things are left to the integrity of the reporter and would this not also apply in this case?

MR. SEDGWICK: Well it might, and that, of course, depends on how wide is the acceptance of the legislation. If the storm raised by the legislation is very great you may never come to that point. As for example some portions of Mr. Walter Gordon's budget which were just not swallowable. You never know how broad a storm you may raise. Of course you have to weather that storm before you come to the point you mention of acceptance.

THE CHAIRMAN: Isn't that what Mr. MacGregor said this morning? Even though I think these things are all possible and good you must sit down with the people who are going to apply this and make sure that they are agreeable, that you can work out your difficulties.

MR. IRWIN: This is quite true. You

have to have acceptance by the community.

THE CHAIRMAN: I think Mr. Irwin is content that we can come up with a formula or four or five methods which won't place an impossible burden on the business community. You have arrived at that position?

MR. IRWIN: That is my considered opinion, yes.

THE CHAIRMAN: Well, gentlemen, this meeting, unless there are any other questions, this meeting is adjourned, but I would like you to come back in five minutes. We have just a few things to discuss. It won't take very long. This is a meeting of the Committee with no transcripts taken.

---WHEREUPON THE MEETING ADJOURNED UNTIL 10:00 A.M., OCTOBER 28, 1964.
